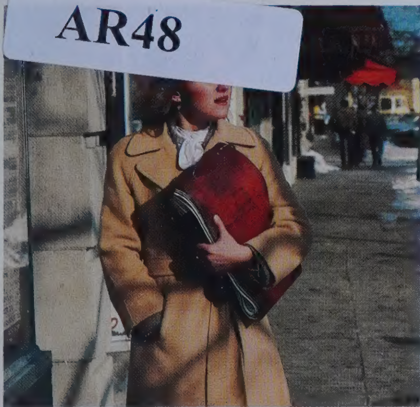
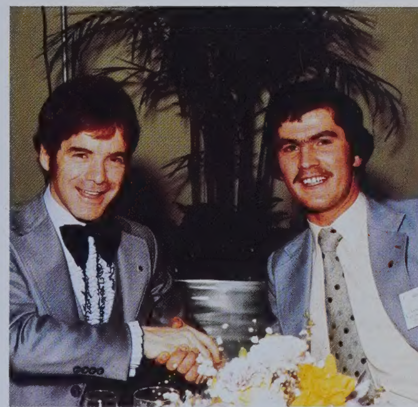
1980 Annual Report





Combined International Corporation

About The Company

Combined International Corporation is a profitable, growing company noted for a success formula, motivational techniques and the organization's Positive Mental Attitude—elements that will lead to future growth of the order achieved in the past.

The company has its origins in a business founded nearly 60 years ago by W. Clement Stone, who continues to serve the company as its chairman.

Earlier results suggest the future prospects. For example, since 1975:

- Direct written premiums have grown at a 10% rate
- Earnings per share up more than 90%
- Dividends per share are 136% higher
- The investment income increase in 1980 was nearly equal to the total earned in 1975
- Return on equity has averaged over 20%

Combined's record reflects its unique marketing system and its line of income protection and life insurance products specifically designed for and sold to particular market segments.

The selling system, known the world over as "The Success System That Never Fails," has produced outstanding results here and abroad, in different economic environments and circumstances. From inception, the accent has been on direct marketing—first of accident and later of health and life insurance products.

Combined uses both forms of direct selling: In-person solicitation (through the Superior Policy Division) and offerings through the mails (via the Agency Division). The great bulk of premium volume is collected in the field by Superior Policy Division sales representatives who contact policyholders every six months, renewing existing policies and offering new or expanded coverages. In this process, the sales person typically solicits new policyholders using the "cold canvass" technique in the business areas of cities and towns.

Combined's primary market is the many millions here and elsewhere who have little if any income protection insurance to provide needed cash when they are disabled. Several factors account for the success of our products:

- convenience of issue
- low unit cost
- non-cancellable
- guaranteed renewable
- fixed premiums
- specific benefits

Combined's life insurance operations also have unique qualities: for example, we offer whole life insurance exclusively, marketed directly by completely separate sales forces in the United States and five foreign territories.

Although accounting for less than 7% of total direct premiums, Combined's Agency Division has developed a special niche in the group accident and health and life insurance business, selling and serving the disability and life insurance needs of hundreds of affiliated groups.

1980 was a year of base-building and problem-solving. The costs and energies devoted to these activities were reflected in growth at a rate much below the long-term potential. However, despite the shortfall, the year ended with evidence that the major goal of our intense and costly efforts had been accomplished. Trained marketing manpower in the field had improved measurably. Since new policy revenues are directly related to the number of people out selling, the manpower trend supports our optimism for the years ahead.

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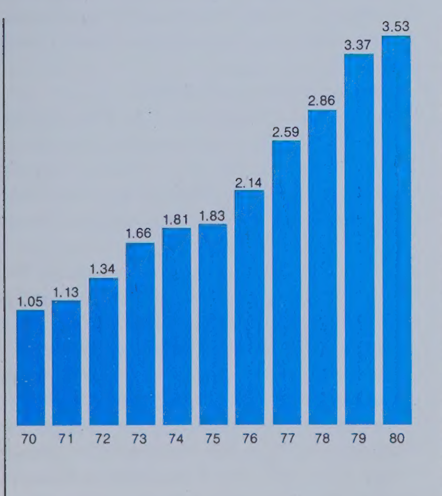
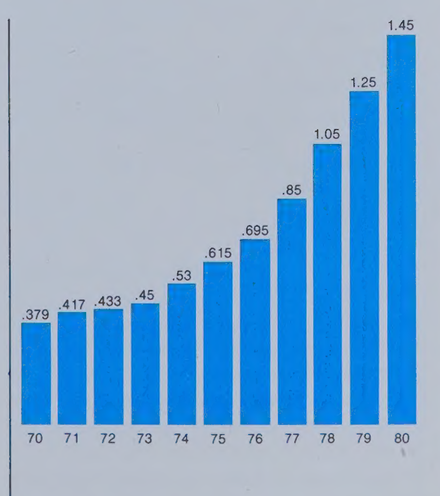
Financial Highlights

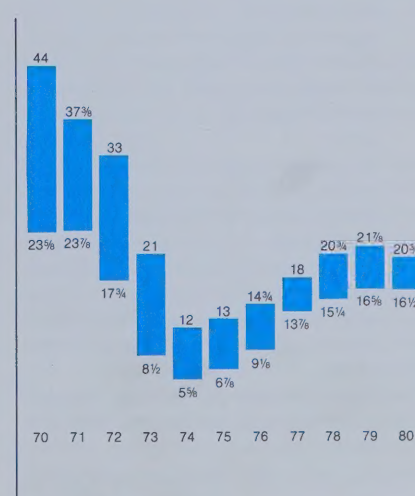
Current Financial Summary	1980	1979	Percent Increase
(000 Omitted)			
Income Before Realized Investment Gains	**$ 95,615**	$ 90,673	5.5%
Per Share	**$3.53**	$3.37	4.9
Net Income	**$ 96,993**	$ 91,006	6.6
Per Share	**$3.58**	$3.38	6.0
Cash Dividends Per Share	**$1.45**	$1.25	16.0
Total Direct Premiums Written	**$ 596,201**	$ 567,549	5.0
Total Direct Premiums Earned			
Accident and Health	**$ 483,482**	$ 463,532	4.3
Life	**109,618**	98,776	11.0
Total	**$ 593,100**	$ 562,308	5.5
Investment Income—Net	**$ 93,813**	$ 68,124	37.7
Financial Position			
Total Assets	**$1,286,896**	$1,157,223	11.2
Stockholders' Equity	**497,379**	442,860	12.3
Stockholders' Equity Per Share	**$18.35**	$16.36	12.2
Direct Life Insurance In Force	**$6,209,149**	$5,471,751	13.5



Earnings Per Share* (in dollars)



Dividends (in dollars)



Price Range* (in dollars)

*Before Realized Investment Gains or Losses.

*Prices prior to May 31, 1980 represent asked prices.

Annual Message to Stockholders

The decade of the 80's has begun auspiciously with a mix of very positive developments and admittedly some disappointments. On the positive side we point to the following:

- Formation of our holding company, Combined International, and the listing of the company shares on the New York Stock Exchange.
- Receipt of our preliminary operating license for Japan.
- Continuation of Combined's long record of consecutive profit and dividend increases spanning more than two decades.
- Completion of our first two portfolio real estate investments, one of which was sold at a $10.8 million gain.
- Continuation of record investment income performance with a 37% increase.
- Good progress in the Agency Division with a 21% premium increase and its important contribution to overhead and profit.
- Another sizable gain in book value per share to $18.35, up from $16.36 a year ago.

On the other hand, domestic A&H and life sales were certainly below minimum expectations. There was insufficient evidence that our measures to restore greater sales vitality to our major businesses had succeeded. Moreover, profits were up a modest 5.5% overall. We intentionally incurred substantial costs investing in future growth, reflected in the general expense increase shown in the analysis following:

Factors in Earnings Per Share Change*

	Total Per Share	% Change in 1980
Premiums Earned		
Direct	$ 21.89	4.9%
Reinsurance	2.58	117.5
Investment Income	3.46	36.9
Total Revenue	$ 27.93	13.6%
Policyholder Benefits	$ 11.66	13.0%
Commissions and General Expenses	11.46	16.0
Loss on Foreign Exchange	.09	N.A.
Provision for Income Tax	1.19	12.9
Earnings per share	$ 3.53	4.9%
Average Shares Outstanding	27,099,792	0.6%

"Earnings per share" means "income after income taxes and before realized investment gains."

As reported earlier, we spent significant sums in formation of the holding company, manpower development, new product and new market expansion. While the final costs exceeded our expectations, the measures were prerequisites to a firm foundation for future growth. A less aggressive attitude might have saved a few pennies per share in 1980, but the cost in reduced future growth would have far exceeded that saving.

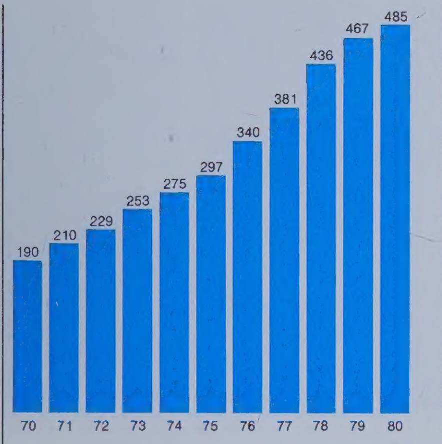
There was a negative swing in foreign exchange results from a gain of $1.0 million in 1979 to a loss of $2.4 million in 1980. The entire subject of such charges is the center of widespread and acrimonious debate in accounting circles and among investors. Revisions of the rules seem a certainty with some favorable implications for Combined.

In summary, we rank 1980 as a non event from the standpoint of bottom line numbers, but a year of marked achievement in many operating areas.

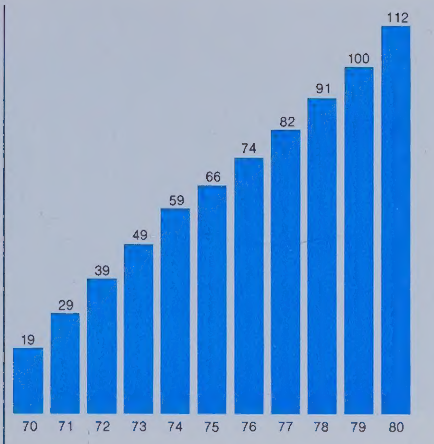
Holding Company Formed

Stockholders approved the Plan of Exchange with Combined International at the annual meeting last April, and it became effective May 30, 1980. Three days later, trading in Combined International shares began on the New York Stock Exchange.

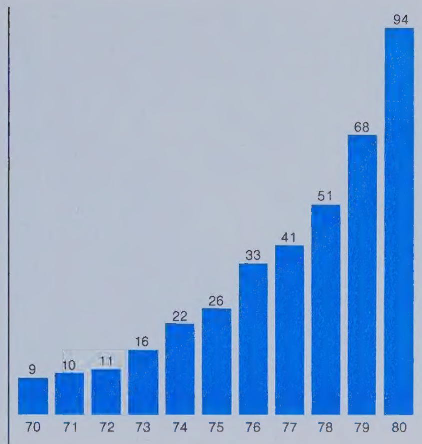
Prior to the annual meeting in 1980 we discussed the rationale for the holding company at some length. Suffice it to say, it was and is our judgment that this new form of organization provides a far greater degree of flexibility than our former operating company status as we contemplate financings and merger/acquisition activity. We do plan future financings, both long and short-term instruments, to facilitate investment programs as well as acquisitions. Combined International's significant borrowing power is a major asset to be developed in the future.



Direct Premiums Written
Accident and Health (in millions of dollars)



Direct Premiums Written
Life (in millions of dollars)



Investment Income (in millions of dollars)

The listing of Combined International shares on the "Big Board" represents an important milestone in our history. The publicity surrounding the opening of "PMA" (the Exchange symbol for Combined International) on the Board was exciting and led to many favorable comments.

New Product Development

Among our latest efforts in the new product category, we would include the adjustable life policy and development and introduction of the Metro Division policy package. These are expensive undertakings, of course, but represent major extensions of our business. Regarded as the most significant innovation in life insurance in this century, adjustable life permits the policyholder virtually total flexibility as to form and amount of life insurance.

The Metro Division was launched in mid 1979 with a mission to develop an entirely new direct marketing insurance business in the major metropolitan areas of the country. In little more than a year this unit has grown to nearly two dozen sales executives and representatives operating in five cities with a completely new line of accident and health insurance products.

We are also engaged in study and experimentation of other new products, sale and renewal methods in all divisions. These include the new life policies for Australia, Ireland and the Japanese markets. In addition, we are running many experiments involving variation in present policy benefit structures and premium levels. As well, it is increasingly apparent that the pre-authorized check method of premium collection is valid for our business.

New Market—Japan

The preliminary Japanese license awarded June 13, 1980 followed two and one-half years of intensive negotiation by our senior management group and hundreds of thousands of dollars of expense. This effort was undertaken because of our conviction that Combined's direct selling methods and products will be unique in that market and will provide us with extraordinary growth opportunities.

The Japanese start-up is a year and a half in the future. The long development phase planned reflects the experience we have had in Europe, particularly West Germany and France. These countries have great promise for the future, but the time necessary to develop top quality resident executives was underestimated in both cases.

Manpower Development

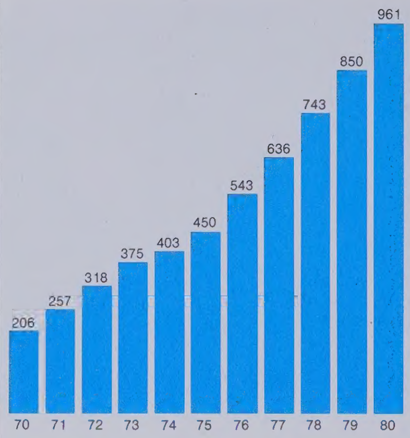
Of the numerous "investments for future growth," the most immediate payoff is from the manpower development program which was given first priority last year. Recruiting quality people, training, motivating and compensating our sales force are key to growth in premiums and profitability, whether domestically or in the international sphere. In the last few years our manpower program has been diluted somewhat by the emphasis on product and area expansion. It is most evident in the Domestic A&H premium growth rate which has averaged only 2% annually in 1979-1980 compared to the 14% average in the later 70's.

In the spring of 1980 we again gave primary focus to the manpower development side of our business, inaugurating a helpful manpower program in the third quarter. Considerable incentives were given. This approach has resulted in numerous manweek records since the end of the third quarter in the U.S. market as well as most of the international areas. We are enthused and believe that our "investment" in this area will pay off.

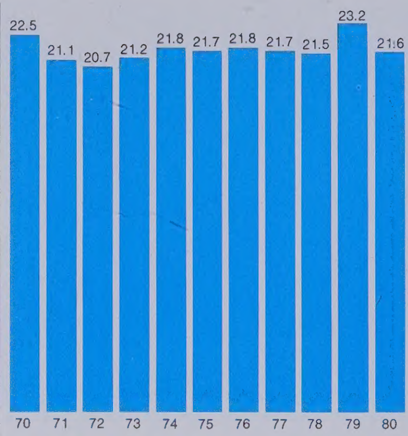
Cash Dividend Prospects

Combined takes great pride in its dividend record over the years. We have increased cash dividends in 29 consecutive years through 1980.

As the chart on page 1 shows, per share dividends increased from 61.5 cents in 1975 to $1.45 in 1980, an increase of 136%. At the same time, earnings per share rose by 93% from $1.83 in 1975 to $3.53 last year. The payout ratio has increased over the period from about 33% to 41% in 1980. As indicated in the past, it has been our policy to limit our dividend payout ratio to the 30-40% range. This policy reflects our desire to maintain the reinvestment rate to finance future growth. We are optimistic about an operating earnings improvement which can then lead to dividend increases.

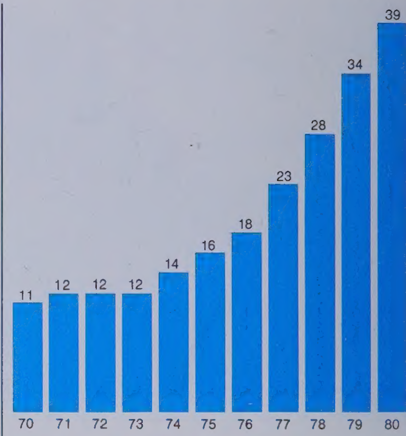


Average Invested Assets (in millions of dollars)



Return on Beginning Stockholders' Equity* (per cent)

**Calculated using Income Before Realized Investment Gains or Losses.*



Cash Dividends (in millions of dollars)

Goals and Objectives

Our longer term objectives stated in their simplest form are:

- To produce above average growth of revenues, profits and dividends for our stockholders.
- To provide a healthy exciting environment in which our people can develop and utilize their interest, skills and capabilities.

You will be interested in our specific goals through 1985 for premiums and various profit factors:

	Annual Growth Objective
Written Premiums	
Domestic A & H	10-15%
USA Life	10-15
International A&H and Life . .	14-21
Agency	9-14
Investable Assets	15+%
Aftertax Return on Stock-holders' Equity...........	20%
Dividend Payout Ratio	30-40%

The realization of these objectives would produce profits per share in excess of $6.00 in 1985 and cash dividends of more than $2.00 per share, exclusive of any contributions from future acquisitions. These figures are exciting to consider, but planning and contemplation do not necessarily translate directly into achievements. The major ingredient is thoughtful action.

Specifically, as to the premium growth goals, we intend to continue our emphasis on:

- Increasing new policyholders.
- Expanding the coverage offered existing policyholders.
- Introducing new policy forms.
- Increasing premium rates where appropriate.

For example, in addition to USA Life's adjustable life form, Metro and international expansion, we are now launching a 50% increase in the coverage of the Domestic A&H Disability Income Amendment. This involves adding a half unit of coverage for $12.50 additional premium semi annually, raising the underwriting limit from the $25.00 premium level to $37.50 for each policyholder. This has strong potential in premium volume terms and commission income in the field.

The specific goals enumerated above do not include any assumptions as to mergers and acquisitions. Our overall goals require an effective program in this area. Our immediate attention is focused on specialty areas of the insurance industry, both life and fire and casualty. We remain flexible in our thinking as to the financing of acquisitions as well as product, geographic areas and alternative selling systems. It is difficult to predict the timing of acquisitions. We have no doubt that important new directions for Combined will evolve in the near future from this source.

Finally, our financial goals will be achieved only with a renewed commitment to effective expense and budget control. This applies to sales and departmental expenses in addition to all of the other costs entering into the profit equation. There is a difficult balance to be struck between long-term growth "investments" and short-term profit results. We intend to apply considerable management attention and discipline to this area.

We wish to extend our thanks to our associates in Combined International worldwide, both in sales and administration, for their efforts this past year. Their talents, positive attitude and actions make all the difference.

W. Clement Stone

W. Clement Stone
Chairman and Founder

Clement Stone

Clement Stone
President and
Chief Executive Officer

Sales System and Products

Success Sales System

More than 6500 Combined Insurance sales representatives are selling and renewing our accident and sickness and life insurance products in the United States and eight international sales territories. Policies vary in detail from one country to another, but the direct selling system is universally used. We refer to that system as the "Success Sales System" because it has stood the test of time through prosperity and recessionary periods in many parts of the world.

Whether it be Sioux Falls, South Dakota, Dublin, Ireland or Auckland, New Zealand, our people are trained to begin their day at the centers of influence in the business, residential or farming districts. They proceed to renew existing policies, sold or renewed six months earlier, and to solicit new policyholders as they move systematically through the area. In many instances they are part of a small team of sales people. Our representatives are 100% commissioned and have as field support a sales manager plus other levels of sales management.

The key to any successful sales organization, of course, is people who are well trained, know their products, are strongly motivated and managed effectively. The "Success Sales System" is organized to produce large numbers of policies sold by such people. And for the many sales representatives who prove themselves in the field, there is the prospect of rapid advancement into sales management positions and beyond.

For example:

John Foote, hired May 1980 in Domestic A&H

- *Promoted to sales manager July 28*
- *Promoted to district manager in December*
- *Has sold 100 or more new policies per week for 26 weeks*

Our people training and motivational techniques are virtually identical around the world. After being recruited, the sales trainee enters a training program and is taught the basics of the system in two, or perhaps, three weeks' time. After being licensed he or she joins the field organization for intensive on-the-job field training.

Of overriding importance to each of our successful representatives is learning the principles of self-motivation and how to acquire and maintain a Positive Mental Attitude. While the results may seem unbelieveable to those who haven't witnessed them, there are thousands of cases in Combined that prove the soundness of the PMA formula which helps people develop a strong self image so that success becomes an expectation and even a habit.

PMA Success Stories

Tom Marsland started in Life Sales December 1979

- *Wrote more than 1500 new life policies in 1980*
- *Top award winner*
- *Promoted to territory manager*

Bernie McGuirk joined the Irish accident team in May 1979

- *Set new world weekly record for introductory policy sales with 660*
- *New records for string writing:*
  600 or more for two weeks
  500 or more for three weeks
  300 or more for four weeks
- *Promoted to sales manager*

John Copeland joined U.K. life in March 1980

- *Wrote 2031 new life units for year*
- *String of 30 consecutive weeks of 50 or more new life policy sales—a record for the U.K.*

Combined's sales people sell low cost supplementary policies providing income protection insurance as well as life coverage. All of our accident policies are issued directly to policyholders upon purchase and do not require home office approval. This is usually described as a "pre-issue" type of policy. As to life and health policies, some very simple qualifying questions are asked of the potential customer to establish eligibility.

"Income protection" is the primary feature of our accident and health products. Nearly all policy benefits are fixed cash sums (indemnities) paid to the policyholder for each day or month of hospitalization or disability as a consequence of accident or sickness. There are convalescent benefits typically provided in these policies also. The income benefits provided are fixed daily or monthly cash payments covering hospital stays and extended periods of convalescence while the insured is disabled.

In summary, our sales representatives are equipped from the start to succeed in the business. They are well trained to sell low cost products that sell in volume and renew in volume.

They are highly motivated and are taught the principles of success. It is a fact that virtually every top sales executive in the company has started in the field selling accident income insurance in stores, offices and banks.

Accident and Health Products

The domestic and foreign branch units of Combined's Superior Policy Division sell and renew a variety of accident and health policies. The introductory policy sold in the United States is an all-accident hospital indemnity policy the coverage of which is later supplemented by a disability income amendment. The detailed description of this policy and the amendment is presented on the opposite page.

The introductory policy sold in all foreign units is a limited-benefit, accident-income policy typically covering common carrier travel, automobile and pedestrian accidents only. At renewal time six months later, the policyholder is offered a full coverage accident insurance policy which is not limited as to type of accident. In the majority of cases the holder of a travel accident policy converts to the full coverage form when it is offered.

Each of these accident policies referred to is noncancellable and guaranteed renewable. In other words, Combined will renew any accident policy no matter how many claims are filed by a policyholder. Additionally, the policy premium rate is fixed and cannot be increased nor can the benefits payable be reduced. According to a leading industry source, Combined Insurance Company of America is the world's largest issuer of noncancellable and guaranteed renewable accident insurance.

In addition to the domestic accident policy and amendment outlined on the upper portion of the opposite page and the other accident policies sold and renewed here and abroad, Combined sells a line of sickness disability or sickness income protection policies. The principal benefits payable under each of these policies are highlighted on the opposite page also.

Life Insurance Policies

Combined now sells life insurance in the U.S. and five foreign sales territories. Policies sold abroad are patterned closely after the domestic product which is a non participating whole life policy.

The U.S. policy is currently offered in $1800 or $3600 amounts (face value) to anyone in good health less than 59 years of age. A most important feature of the policy is the policyholder's option to increase the face value coverage up to five times the original face value, *i.e.*, to $9000 or $18,000. The option to amend is granted to each policyholder who qualifies according to the applicable underwriting standards. No physical examination is required in connection with the amendment election. Other policy features include:

- Variety of settlement options.
- Cash values beginning the second year the policy is in force.
- Cash policy loans available at 6% interest; automatic premium loan option.
- Waiver of premium during period of total disability.

Combined also offers in the U.S. a Senior Citizens life insurance policy in $1800 or $3600 face value denomination to persons 60 to 75 years old who qualify under the applicable underwriting standards. This policy form is not amendable but the benefits closely parallel the regular life policy as to cash settlement options, cash values, policy loans and automatic premium loans.

The adjustable life policy form is discussed elsewhere in this report. It should be noted that the policy is sold only to holders of our standard life policy in the United States.

Domestic Accident Policy Premiums and Benefits

	All Accident Hospital Indemnity Policy	Hospital Indemnity and Disability Income Amendment
Total Semiannual Premium	$20(1)	$45(1)
Policy Benefit by Type:	Cash Benefit Payable if Injured	
Hospital confinement	$30 per day(2) $900 per month	$30 per day(2) $900 per month
Convalescent care	$15 per day(3) $450 per month	$15 per day(3) $450 per month
Medical expense	Optional to $20 per accident	Additional to $20 per accident
Total disability		$200 per month up to 6 months
Loss of life, sight or limbs		$3000 loss of life or double loss of eyes or limbs

Domestic Health Care Policy Premiums and Benefits

Sickness Disability Income Policy
($72 semiannual premium (1))

- *$200 per month up to six months when totally disabled due to sickness, confined or not.*
- *$100 when partially disabled due to sickness.*
- *Triple the $200 monthly benefit to $600 for up to six months when insured is confined in a hospital.*

Sickness Hospital Indemnity Policy
($84 semiannual premium (1))

- *$30 a day for each day of hospital confinement for sickness up to 365 days.*
- *$30 a day for each day while confined to an intensive care unit.*
- *$15 a day for total disability following hospitalization due to sickness.*

Combined Cancer Hospital Indemnity and Surgical Expense Policy
($60 semiannual premium for family and $40 for individual)

- *$100 cash payment per day of hospital confinement caused only by cancer up to 500 days or $50,000.*
- *Surgical benefit up to $50 times the number of days confined up to maximum of $1,500.*
- *Benefit up to $1,000 maximum for X-ray therapy treatment, radium, cobalt when not confined.*

(1) For full unit. Policy and Amendment also sold in half units with benefits half those indicated.
(2) For lifetime if necessary plus accumulation.
(3) Up to same number of days hospitalized.

Superior Policy Division

Total premiums written for the three direct marketing units was $551 million in 1980, up 4.2% from the 1979 level. Discussion of results for each unit and new developments follow in subsequent paragraphs.

Domestic Accident and Health

Premium volume in 1980 totaled $332 million, down 0.6% from the 1979 level. By any measure this past year was our most disappointing year in many years. Not only did premiums fail to reach our targets, but our profitability was reduced because expense budgets had been geared to a higher volume of business.

In mid 1979 we set out to improve sales proficiency of our sales forces, both Accident and Health Care. This required new emphasis on the company's basic marketing methods, namely, selling systematically "down the street" in business places. From the very beginning the company's business, of course, had been based on successful "cold canvass" selling techniques.

We accomplished one important objective, that being an increase in *new sales* proficiency per man. Sales proficiency did, in fact, improve in 1980, rising from 13.5 per man in 1979 to 15.8 per man in 1980. This is very important because our business can only prosper with an expanding policyholder base.

In this return to basics approach, we suffered some major manpower losses. Many sales representatives could not or would not follow the system. In the spring of 1980 it was apparent we faced a real manpower shortage. We undertook a program to boost manpower to a new record level by the end of the third quarter. This effort was successful and in the final week of that quarter we had 4200 representatives in the field selling accident insurance. This compared with some 3300 at the beginning of 1980.

For 1981 we are planning to augment the product line by adding an additional half unit of the disability income amendment with a $12.50 semiannual premium. Thus, all of our policyholders with a Hospital Indemnity Policy will be able to add more disability income coverage. Our sales representatives will benefit from the standpoint of commissions, which is an important consideration.

It is our plan to authorize annual changes in amounts of various coverages our people can offer to the policyholders. This can take a variety of forms but is best illustrated in reference to a change now being implemented for the Sickness Income Policy. Where authorized, the monthly disability benefit has been raised 50% in certain states from a $200 per month benefit (full unit) to $300 with a corresponding increase in premiums. This type of change not only updates the policyholder's protection but provides the sales force the greater commission potential also.

Our new national sales manager, Michael Hester, and his staff of divisional and field sales executives are enthused about their prospects in the new year. They believe in the business, they are in good selling trim and can make it happen. Their "aim-high" goal is to produce a premium growth rate in double digit figures this year and thereafter.

International Operations

The year 1980 was comparatively favorable for International with premiums up 16.7% in U.S. dollar terms (13.0% in comparable currencies). The margin of profit increased also which is particularly satisfying in this era of rampant inflation everywhere.

Again in 1980, the best premium growth rates were achieved in the U.K. (+30%) and Ireland (+28%), both countries with extensive national health programs. Still, solid progress was scored in Canada, Australia and New Zealand.

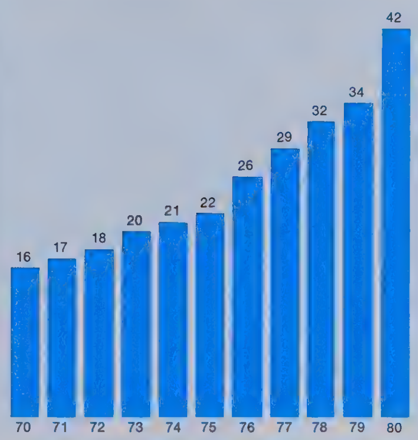
International operations achieved new manpower records in the second half of 1980. Our objective all along has been to be at full strength in field manpower terms as the new year begins.

Life insurance sales are underway in five of the international territories (including Hawaii), Australia being the latest. Total life premiums written were $18 million in 1980, up 36.3%. The outstanding U.K. results are continuing. We are now forming a life insurance subsidiary in Ireland preparatory to undertaking life operations there.

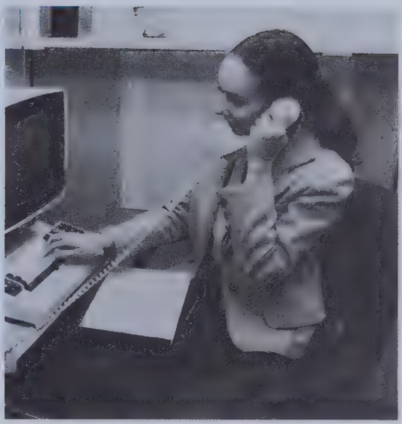
The receipt of our preliminary Japanese license was one of the most exciting events of the last year. The license authorizes Combined to sell life insurance, and we have developed a unique life policy which incorporates a variety of accident, disability and life benefits. This form may well be the forerunner of policies we will offer elsewhere in the world.

Our present plan is to begin operations in Japan in 1982 when we hope to be adequately staffed and trained. This will require the patience and hard work of many people in the organization. We believe the rewards to stockholders and Combined people will justify the investment to be made for several years. All in all, prospects are bright for Inter-

Agency Division



Agency Division Premiums Written (in millions of dollars)



national operations assuming the sales and administrative leadership functions up to potential in all units.

Domestic Life

Domestic life insurance premium volume in 1980 exceeded $91 million, increasing 7.1% from the 1979 level. Virtually all of the gain in premiums this past year has come from our adjustable life policy introduced on a production basis in 1979. It is noteworthy that we had more than $936 million face value of this new form in force at the year-end. This is a substantial amount of business in such a short span of time.

Since its introduction we have had a number of major individual sales records set with the adjustable life policy. As an example, one of our sales representatives from Illinois sold:

$1,000,000 face value in 11 days . . .

$3,000,000 face value in 10 weeks . . . and

$8,900,000 face value for the year!

It should be noted that the life insurance industry has traditionally recognized those individuals who sell $1,000,000 face value in a year . . . and less than 2% do that.

Adjustable life premiums were $10 million in 1980, in this our first full year of sales.

At the end of 1980 we had $6.2 billion of life insurance in force on a worldwide basis, an increase of 14% from the prior year-end. Domestic life insurance accounted for about 78% of the total insurance in force.

The Agency Division markets accident, health and life coverages by mail to groups of affiliated persons. Division premiums have grown at the compound rate of 14% per annum since 1975, reaching $42 million in 1980. This has been a highly productive period characterized by declining loss ratios, a well-controlled expense structure and development of a reputation for administration and service in the disability insurance field.

The Division's principal products include long-term disability insurance, term life and accidental death, as well as hospital indemnity coverage. In many respects these coverages parallel those of the Superior Policy Division's domestic A&H and Life operations in the sense that they involve income protection or life insurance benefits. On the other hand, Agency Division policies are by their nature *primary* insurance coverages rather than *supplementary*. For example, Agency's term life and accidental death benefit can reach a maximum of $250,000 compared to the standard domestic life maximum coverage of $18,000.

The Agency Division market includes three primary groups:

1. Small employers with employees enrolled in their respective coverages by direct mail through sponsored groups such as trade associations.
2. Medium and small employers without group affiliation who are enrolled by local insurance brokers.
3. Individuals who are enrolled in a group insurance program by direct mail through sponsored groups including professional associations, credit cards, etc.

Thus, the primary elements of the Agency business are groups of people, affiliated in one fashion or another and solicited via the mails. Of course, these solicitations are preceded by endorsements arranged by our own highly qualified sales unit which calls on local brokers and sponsoring groups. In virtually all cases there is an insurance broker involved with sponsoring groups.

The Division is not unusual in the industry in terms of products. However, Agency does involve a unique blend of organization of marketing and administration.

Moreover, the Agency Division now has its own electronic management information and administrative system supporting a highly effective personalized service handling operation. This is the heart of a responsive service organization which requires nearly instantaneous information such as employee and dependent status.

The Agency Division Claim Department has earned a top reputation as an outstanding administrator of long-term disability claims. This is the most difficult and most interpretive part of employee benefit handling. Our operation includes:

- A specially trained unit recognizing the employer concerns when handling the claims of disabled employees.
- Realistic constructive rehabilitation services.
- Expertise which is recognized and sold to other insurance companies through reinsurance and administrative service contracts.

We are confident of the Division's future as an imaginative underwriter and program administrator.

Investment Operations

Year	Average Invested Assets (000)	Net Investment Income* (000)	% Yield On Average Invested Assets*
1980	**$961,251**	**$93,813**	**9.76%**
1979	850,357	68,124	8.01
1978	742,734	51,425	6.92
1977	636,069	40,565	6.38
1976	542,549	32,723	6.03
1975	450,250	25,948	5.76

**Before Income Tax .*

1980 Results

The year 1980 was another year of solid progress in investment operations. The highlights are:

- Net investment income rose nearly 38% to $93.8 million.
- Yield on average invested assets improved sharply for the 8th consecutive year, rising to 9.76% from 8.01% for 1979.
- Invested assets were almost $1 billion, averaging $961 million last year.
- Sale of our first portfolio real estate investment resulted in a $10.8 million capital gain.

Included in our $93.8 million investment income figure is additional interest of $2.9 million flowing from a recent real estate investment discussed below. Suffice it to say, without this extra profit, investment income would have totaled $90.9 million, still almost 34% above the prior year.

We are pleased with these results, of course, but not the least complacent. 1981 comparisons will be tougher than usual.

In the longer term perspective the company portfolio has made great strides in terms of percentage yield and income production. For example, in the 1970-80 period, investment income grew from $8.7 million to $93.8 million, a compound annual rate of 26.8%. This compares with the 12.7% compound growth rate estimated for the life insurance industry in the same period.

Similar comparative results can be reported for yield on average invested assets, a measure at least in part indicating the efficiency with which funds are invested. During the last 11-year period Combined's pretax yield on average invested assets has increased from the 4.22% level in 1970 to 9.76% for the year 1980. It was not until 1979 that Combined's return exceeded the industry average and the margin in favor of Combined continues to widen. These results are highlighted in the table below.

Yield on Invested Assets*

	U.S. Life Industry	Combined
1970	5.34%	4.22%
1972	5.69	3.59
1974	6.31	5.40
1976	6.68	6.03
1978	7.39	6.92
1979	7.78	8.01
1980	8.02e	9.76

**Net investment income divided by average invested assets.*

The company's investment progress as measured by the growth of investment income and portfolio yield reflects two major factors: (1) the above average rate of growth in the company's invested assets (nearly 5-fold versus the 3-fold gain for the life industry) and, (2) an investment strategy in recent years which has emphasized the short-term sector of the fixed interest market where the most dramatic yield increases have materialized. The rapid asset growth, of course, is directly attributable to Combined's marketing departments, their premium volume growth and profitability. Domestic life premium growth, in particular, has made a major contribution to the asset base because virtually the entire book of business is whole life insurance.

Asset Mix

The table at the top of the opposite page presents the percentage breakdown of Combined's invested assets for the six-year period 1975-1980. The most noteworthy changes are the following:

1. The invested cash position has increased markedly from the 1975-1977 average reflecting our continuing concern about interest rates from late 1977 to the present.
2. The policy loan percentage has grown but is a minor factor in the portfolio mix in contrast to the life insurance industry as a whole.
3. The common stock position has been maintained in the 14 to 20% range.
4. Preferred stocks have been deliberately reduced whenever possible in the years after 1977. This trend will continue.
5. The bond category has been maintained in the 54-61% range in the last four years, but the average life (maturity) was shortened from 8 years in 1977 to 6 years in 1979. The average life of the bond portfolio was extended to 12 years as of year end 1980 to take advantage of peak interest rates.

Year	Bonds And Notes At Amortized Cost	Preferred Stock	Common Stock	Mortgage Loans And Real Estate Net Of Accumulated Depreciation	Policy Loans And Other	Invested Cash
1980	**60.8%**	**7.5%**	**14.1%**	**4.0%**	**2.1%**	**11.5%**
1979	57.4	8.4	18.2	2.4	1.6	12.0
1978	54.5	11.6	15.1	2.3	1.5	15.0
1977	53.9	19.1	20.2	1.9	1.4	3.5
1976	61.6	13.7	19.7	2.3	1.2	1.5
1975	63.2	13.3	17.8	2.4	1.1	2.2

The maturity breakdown of the bond account (exclusive of commercial paper) is presented in the table following:

Consolidated Bond Maturity Schedule
December 31, 1980

		% of Total
Maturing in 1981		7%
Maturing in 1982		4
Maturing in 1983		4
Maturing in 1984		8
Maturing in 1985		5
Total	1 - 5 Years	28%
	6 - 10 Years	12
	11 - 15 Years	30
	Over 15 Years	30
	Total	100%

Investment Environment and Investment Strategy

We have already alluded to the investment environment which has prevailed over the last several years and our adaptation to it. The last eleven years have been characterized by accelerating inflation and an increase in the volatility in the securities markets, particularly interest rates. Almost everyone agrees that continuation of these trends will be ruinous and lead to massive changes in our economy and possibly a major cyclical downtrend. We applaud the efforts now underway to change the unfortunate course of national economic policy, both fiscal and monetary.

In the meantime, we continue to have a cautious view of the markets, putting great value on liquidity and investment flexibility. Looking ahead for the next two or three years, there are no plans for major shifts in investment policy. If anything, we will tend to favor equities of one form or another and maintain a fairly conservative bond strategy.

The real estate investment program begun in 1979 produced surprisingly favorable results in 1980. In mid 1979 we committed to finance the equity interest in an office building complex in Los Angeles in exchange for 50% interest in the project. The details aside, we finally funded a $6.6 million investment in the spring of 1980. Immediately thereafter, a cash offer for about 78% of the building was received, and, along with our partner, we agreed to sell. The transaction was closed in September 1980 at which time we received payment of our investment of $6.6 million and a cash profit of $10.8 million. In addition, we retain an 11% interest in the building which will have great value down the road. Needless to say we were thrilled by these results.

One other investment was made in the early summer involving a large condominium conversion project on the east coast. In this instance we loaned funds to a partnership to purchase and renovate the building. Our returns from the project take the form of interest on our loan as well as additional interest equal to 25% of the ultimate conversion profit. As was the case of the Los Angeles building, the condominium project has become quite a success. Nearly two thirds of the units were sold in the initial selling period ended in October. The balance of the property likely will sell before the current year is over. Because of this noteworthy success, we have reflected $2.9 million additional interest in net investment income for 1980. This amount is approximately 40% of the total gain expected upon completion of the conversion.

We look forward to the prospect of many real estate successes in the future. In the meantime we are attempting to build a competent staff to handle this activity. There appear to be many meritorious opportunities around these days and there should be no problem placing $20 million or more annually in selected income properties.

1981 Investment Prospects

The new year is expected to be a year of continued good growth in the asset base and net investment income. The rate of increase in net investment income will surely be less than that experienced in 1980, primarily because of declining market yields and the exceptional 1980 increase.

We anticipate 1981 will be a year of lessened inflation and lower interest rates. Our efforts will be directed towards capitalizing on these circumstances to the maximum extent possible.

Description of the Business

Company Development and Structure
Combined International Corporation was formed last year to facilitate diversification into new areas of financial services and the optimum use of the very strong Combined Insurance balance sheet, both without disturbing the marketing systems so favorable to the extended growth of the traditional business. Established in 1922, Combined has enjoyed several decades of uninterrupted growth as a specialty insurer principally through direct marketing of low cost, supplemental insurance to all segments of the population.

The *Success System That Never Fails,* developed by the chairman and founder of Combined Insurance, W. Clement Stone, was and is a key to that development. W. Clement Stone's record of growth was extended by Clement Stone who became president in 1971 following many years in various capacities with Combined Insurance. As president of the United Kingdom operations the unit recorded a 100% average annual increase in written premium and dramatic earnings growth during his seven years in that position.

At year-end 1979 the net result of that joint leadership was a company with:

- An outstanding position in its particular specialty
- An effective and experienced top management
- Proven marketing ability
- Demonstrated investment management expertise
- Unused financial leverage

The formation of a holding company enables Combined to begin undertaking a broader range of insurance, investment and other activities than is permitted companies operating under the insurance code of the State of Illinois. The holding company is a prerequisite for the fullest realization of Combined's growth potential from available resources, both human and financial.

Therefore, Combined International Corporation was formed under the laws of Delaware to hold as its principal asset the common stock of Combined Insurance Company of America, which became a wholly-owned subsidiary. The holding company structure was approved at the 1980 annual meeting of stockholders and became effective May 30, 1980. Combined International

Business Segment Growth and Trends
The past contribution of major product lines and geographic areas to total revenues and pretax income are a basis for understanding past results and assessing future prospects.

Combined Insurance is engaged in three business segments. Accident and health coverages are the foundation of the company's past growth. In recent years life revenues have grown somewhat more rapidly. The company's excellent financial condition along with the availability of attractive reinsurance treaties has led to the sharp growth of reinsurance premiums. The different rates of gain have caused a shift in the relative contribution of the major product lines, as illustrated in the chart following.

Major Product Lines

($ in millions)

	Years Ended December 31*											
	1980		1979		1978		1977		1976		1975	
	Amount	**% to Total**	Amount	% to Total	Amount	% to Total	Amount	% to Total	Amount	% to Total	Amount	% to Total
							(Unaudited)		(Unaudited)		(Unaudited)	
Total Revenue Earned												
Direct Life	**$ 142.0**	**18.7%**	$ 121.1	18.3%	$ 105.1	17.6%	$ 92.3	18.0%	$ 81.6	18.3%	$ 71.1	18.1%
Direct Accident & Health	**544.9**	**72.0**	509.3	76.9	459.0	76.6	397.6	77.7	351.3	78.7	308.5	78.7
Reinsurance	**70.1**	**9.3**	32.1	4.8	34.8	5.8	21.9	4.3	13.6	3.0	12.4	3.2
Total	**$ 757.0**	**100.0%**	$ 662.5	100.0%	$ 598.9	100.0%	$511.8	100.0%	$446.5	100.0%	$392.0	100.0%
Income Before Income Tax and Realized Investment Gains												
Direct Life	**$ 16.9**	**13.2%**	$ 14.1	11.8%	$ 10.6	10.9%	$ 11.6	14.3%	$ 10.0	14.2%	$ 8.8	14.7%
Direct Accident & Health	**108.6**	**84.8**	103.8	87.1	85.0	87.7	68.4	84.5	59.5	84.8	50.7	84.6
Reinsurance	**2.5**	**2.0**	1.3	1.1	1.3	1.4	0.9	1.2	0.7	1.0	0.4	0.7
Total	**$ 128.0**	**100.0%**	$ 119.2	100.0%	$ 96.9	100.0%	$ 80.9	100.0%	$ 70.2	100.0%	$ 59.9	100.0%

**The above results include allocations of investment income and certain expense elements considered reasonable under the circumstances. It should be understood that other acceptable methods of allocation might produce different results. Total revenues and pretax income exclude realized investment gains and losses, but include net investment income.*

Combined's first venture abroad was in 1956 with the establishment of operations in Canada. Subsequent expansion included:

Country	**Year Established**
Australia	1960
United Kingdom	1964
New Zealand	1965
Republic of Ireland	1976
West Germany	1976

In the recent past, International revenues have grown more rapidly than domestic, while the proportion of pretax income in both areas has remained fairly stable.

A substantial expansion of International operations is expected through growth in most areas where we are presently represented and through expansion into new areas such as Japan.

shares were listed on the New York Stock Exchange for trading effective June 2, 1980.

The substantial financial resources of the company give substance to the announced intention of growth in part through acquisition—a process in the active planning stage for which the following criteria have been established:

- Must be in the financial services business, preferably insurance related
- Will be acquired for cash or some equivalent
- Will be acquired on a friendly basis
- Must provide for existing management to remain in place.

Future acquisitions can be accommodated easily in the holding company, which is seen primarily as a vehicle for that purpose and not as an operating entity.

As presently constituted, the four domestic marketing groups, International operations, reinsurance and investment operations are the revenue sources of the company. While the domestic marketing groups function as divisions relying on separate staffs for accounting and administrative services, International operations is essentially a group of separate entities, each with its administrative staff and sales department.

The overall growth goals are determined annually through the comprehensive sales plan. Achievement of the targets agreed on is both encouraged and recognized through incentive compensation plans. The annual sales plan is developed by sales management, with input from various management levels.

The plan is reviewed by top management in the light of the available manpower and long-term goals, thereafter becoming a commitment of each marketing organization and individual within it. (The sales methods employed have been described in *Success Sales System*, page 5.)

The sales plan is constructed in terms of written premium goals with respect to product lines, new sales and renewals. The compensation plan is fundamentally a blend of commission and bonus, in cash or merchandise, plus recognition. The plan structure is adjusted as necessary to accomplish the sales plan goals.

Domestic vs. International Results

($ in millions)

	Years Ended December 31											
	1980		1979		1978		1977		1976		1975	
	Amount	**% to Total**	Amount	% to Total	Amount	% to Total	Amount	% to Total	Amount	% to Total	Amount	% to Total
							(Unaudited)		(Unaudited)		(Unaudited)	
Total Revenue Earned												
Domestic	**$ 621.6**	**82.1%**	$ 550.0	83.0%	$ 505.7	84.4%	$430.9	84.2%	$371.7	83.2%	$327.2	83.5%
International	**135.4**	**17.9**	112.5	17.0	93.2	15.6	80.9	15.8	74.8	16.8	64.8	16.5
Total	**$ 757.0**	**100.0%**	$ 662.5	100.0%	$ 598.9	100.0%	$511.8	100.0%	$446.5	100.0%	$392.0	100.0%
Income Before Income Tax and Realized Investment Gains												
Domestic	**$ 109.2**	**85.3%**	$ 102.6	86.1%	$ 84.3	87.0%	$ 71.0	87.8%	$ 59.2	84.3%	$ 51.4	85.8%
International	**18.8**	**14.7**	16.6	13.9	12.6	13.0	9.9	12.2	11.0	15.7	8.5	14.2
Total	**$ 128.0**	**100.0%**	$ 119.2	100.0%	$ 96.9	100.0%	$ 80.9	100.0%	$ 70.2	100.0%	$ 59.9	100.0%
Total Assets (At End of Period)												
Domestic	**$1,107.1**	**86.0%**	$1,000.5	86.5%	$ 887.6	87.4%	$762.7	86.0%	$658.5	85.6%	$536.8	84.8%
International	**179.8**	**14.0**	156.7	13.5	127.6	12.6	124.4	14.0	110.7	14.4	96.0	15.2
Total	**$1,286.9**	**100.0%**	$1,157.2	100.0%	$1,015.2	100.0%	$887.1	100.0%	$769.2	100.0%	$632.8	100.0%

Although Combined's direct selling methods and products are, in management's opinion, applicable to all cultures, some significant refinement may be required in observance of local law and custom. The life policy to be sold in Japan is an example of the benefit to be gained from creative adjustment. The preliminary license was granted on the condition that Combined Insurance answer a need that other insurers did not fulfill. Therefore, in consultation with Japanese insurance regulators, we devised a new life policy form with various benefits as follows:

- Term life policy with specified death benefits at different age levels.
- Disability income benefits payable as a result of certain injuries.
- Hospitalization benefits related to confinement as the result of injury.

There are other countries in Europe and elsewhere where the "Success Sales System" and creative adjustment appear to have application.

An ongoing program to expand into those areas will be conducted and announced as operating authority is requested.

Premiums Written by Product Line

The table below details the growth of premiums written by product line and by marketing unit.

Domestically, the hospital indemnity, sickness and cancer policies have grown more rapidly than limited accident coverage which is being phased out. These popular policies fill the most significant gap in the average person's insurance program—the uncovered portion of many group plans, including Medicare/Medicaid. They help allay the justifiable concern over the possibility of ruinous expense that can accompany prolonged hospital confinement by providing essential income protection coverage.

Premiums Written

(000 Omitted)	1980 Amount	1980 % to Total	1979 Amount	1979 % to Total	1978 Amount	1978 % to Total	1977 Amount	1977 % to Total	1976 Amount	1976 % to Total	1975 Amount	1975 % to Total
Accident and Health												
Superior Policy Division—USA												
Limited Accident	$ 24,149	3.6%	$ 28,806	4.8%	$ 36,001	6.4%	$ 44,504	9.0%	$ 47,917	11.1%	$ 52,608	14.0%
All-Accident-Disability Income	120,762	17.8	131,567	21.8	135,023	24.1	131,127	26.7	125,847	29.2	118,621	31.6
All-Accident-Hospital Indemnity	131,636	19.5	122,264	20.2	107,040	19.2	72,278	14.7	46,247	10.7	24,315	6.5
Sickness	38,532	5.7	35,388	5.9	28,520	5.1	22,740	4.6	19,542	4.6	17,607	4.7
Cancer	17,172	2.5	16,336	2.7	12,877	2.3	8,912	1.8	5,263	1.2	1,105	0.3
Total Superior Policy Division—USA	$332,251	49.1%	$334,361	55.4%	$319,461	57.1%	$279,561	56.8%	$244,816	56.8%	$214,256	57.1%
Superior Policy Division—International												
Limited Accident	$ 22,667	3.3%	$ 20,706	3.4%	$ 19,457	3.5%	$ 18,019	3.7%	$ 16,669	3.9%	$ 14,449	3.9%
All-Accident-Disability Income	60,975	9.0	54,993	9.1	47,772	8.5	40,231	8.2	38,545	8.9	34,946	9.3
All-Accident-Hospital Indemnity	3,926	0.6	3,729	0.6	3,704	0.7	3,170	0.6	3,096	0.7	2,846	0.7
Sickness	20,967	3.1	16,023	2.7	11,506	2.1	9,720	2.0	9,298	2.2	7,539	2.0
Cancer	1,171	0.2	807	0.1	388	0.1	54	—	17	—	—	—
Total Superior Policy Division—International	$109,706	16.2%	$ 96,258	15.9%	$ 82,827	14.9%	$ 71,194	14.5%	$ 67,625	15.7%	$ 59,780	15.9%
Agency Division	$ 37,496	5.5%	$ 31,082	5.1%	$ 29,334	5.2%	$ 26,898	5.5%	$ 23,944	5.6%	$ 20,604	5.5%
All Other	$ 5,127	0.8%	$ 5,357	0.9%	$ 4,611	0.8%	$ 3,836	0.8%	$ 3,136	0.7%	$ 2,370	0.6%
Total Accident and Health	$484,580	71.6%	$467,058	77.3%	$436,233	78.0%	$381,489	77.6%	$339,521	78.8%	$297,010	79.1%
Life												
Superior Policy Division—USA	$ 91,285	13.5%	$ 85,227	14.1%	$ 79,500	14.2%	$ 73,357	14.9%	$ 66,880	15.5%	$ 60,907	16.2%
Superior Policy Division—International	18,143	2.7	13,314	2.2	9,577	1.7	7,297	1.5	5,825	1.3	4,363	1.2
Agency and All Other	2,193	0.3	1,950	0.4	1,756	0.3	1,455	0.3	1,211	0.3	1,087	0.3
Total Life	$111,621	16.5%	$100,491	16.7%	$ 90,833	16.2%	$ 82,109	16.7%	$ 73,916	17.1%	$ 66,357	17.7%
Reinsurance	$ 80,212	11.9%	$ 36,208	6.0%	$ 32,241	5.8%	$ 27,987	5.7%	$ 17,644	4.1%	$ 11,833	3.2%
Total	$676,413	100.0%	$603,757	100.0%	$559,307	100.0%	$491,585	100.0%	$431,081	100.0%	$375,200	100.0%

Competition, Industry Position and Regulation

Insurance is one of the most competitive industries. It is reported there are over 1800 life insurance companies in the United States alone. Many are larger than Combined and have greater financial resources. Many sell accident and health insurance exclusively or in conjunction with other products. And many are mutual companies which some believe have a competitive advantage over stock companies since the profits of mutuals may be passed on to policyholders in the form of lower rates. However, it is also significant that relatively few of the 1800 companies are licensed in all 50 states, as is Combined. Fewer still have specialized in Combined's particular market, employ the direct sales method or field renewal. In its particular segment of the accident and health industry, Combined is the largest issuer of noncancellable and guaranteed renewable individual accident insurance and ranks among the top specialty insurers in the nation.

Creativity and innovation are the factors behind Combined's industry ranking, exemplified by the 1979 introduction of the adjustable life policy in the United States, the development of the unique life insurance product for the Japanese market, as well as the new Metro policy line.

States accounting for the largest proportion of written premiums in 1980 were:

A & H	Life
New York	New York
Iowa	Iowa
North Carolina	Texas
California	Illinois
Texas	Wisconsin

The primary purpose of state regulation of the insurance industry is to ensure that an insurance company will be able to meet all of its obligations as they come due. To this end, the states prescribe a method of accounting and reporting, commonly referred to as "statutory accounting," which emphasizes cash basis and liquidation basis accounting. This does not conform to, and is not intended to conform to, generally accepted accounting principles (GAAP) as they apply to life insurance companies. Combined uses GAAP for reporting to stockholders, other investors and the general public to make the financial statements comparable to those furnished by other companies in other industries.

Combined Insurance prepares statements in conformity with statutory accounting to be filed with the various state insurance commissioners. A reconciliation is included as note 12 of the notes to consolidated financial statements.

Insurance regulations vary from state to state and among different jurisdictions but all affect Combined Insurance in those geographic areas where it does business. In general, state laws cover the granting and revoking of licenses to do business, regulations of trade practices, licensing of agents, policy form approval, reserve and capital requirements, etc.

Additional requirements under state laws require Combined Insurance to file detailed annual reports in all states and jurisdictions in which Combined Insurance does business. Some require audited financial statements as well.

Various states have enacted insurance holding company laws which require registration and periodic reporting by insurance companies licensed to transact business within their respective jurisdictions and controlled by other corporations. Combined is subject to such legislation and responds accordingly.

National Health Care

A number of national health care plans have been proposed, but Combined expects that any plan finally enacted will have little, if any, impact on the company for two reasons: first, Combined Insurance policies pay benefits in addition to whatever benefits are paid by any other plan the policyholder has, and second, national health care proposals are designed to cover only certain costs incurred, leaving some amount to be covered by the insured. For example, various health plans are in effect in the United Kingdom, the Republic of Ireland, Australia, New Zealand and Canada. As indicated, Combined has successfully and profitably marketed its products to supplement the benefits offered by those plans.

Financial Review and Statements

Properties

Combined Insurance owns and occupies office buildings in four states and Puerto Rico, totaling 945,000 square feet. In addition, the company leases offices in 39 cities in the United States and in 20 foreign cities, totaling 651,000 square feet.

The original cost of all property owned by Combined is $29.8 million, with accumulated depreciation of $8.4 million as of last year end.

Combined Insurance owns 39 acres of land for investment and office expansion in Northbrook, Illinois, a suburb of Chicago. A portion is leased to a developer and Combined Insurance is a major tenant in an office building built on this leased acreage. Combined will be the sole tenant of a second building on land contiguous to the land owned by Combined. Over the next decade the company plans to develop the remaining land into a major office complex to be used in part to accommodate the anticipated growth of home office operations.

Management's Discussion and Analysis of Operating Results and Financial Condition

Introduction

Management has long recognized and frequently stated a fundamental long-term goal: consistent, above average growth of premiums, profits and dividends. During the past ten years Combined's income per share before realized investment gains has expanded at a 13% compound rate vs 11% for the S&P 500. Dividends, raised 29 consecutive years, have reached $1.60 per share annually.

To assess the recent past as an indication of the future, an explanation of the earnings growth mechanism is a useful introduction. Earning potential or earning power is determined by the amounts of revenues, assets and equity. The realization of that potential depends on the rates of return attributable to those three determinants.

	Growth Rates			
	1980	1979	1975/80	1970/80
Revenues	**14.3%**	10.6%	14.1%	13.5%
Assets	**11.2**	14.0	15.2	15.5
Equity	**12.3**	13.5	13.8	12.8

In the short run, earnings growth may be achieved by raising the rates of return. But to a company operating at or near peak efficiency, the chief means of growth begins with the reinvestment of earnings.

The rate at which earning power can be expanded depends on two factors: the projected rate of return on stockholders' investment and the proportion of earnings reinvested. In other words, growth depends on profitability and reinvestment of earnings, a relationship expressed by the formula:

Internal Growth Potential = Expected return on stockholders' equity times the percentage of profit retained

As shown by adjoining charts, income before realized gains since 1975 has increased at about 14% compounded annually, which is roughly comparable to the 13% rate for the last decade. An average 64.4% of earnings was reinvested annually and dividends increased at a 18.7% rate since 1975.

Combined's announced intention is to pay out 30-40% of earnings in the form of dividends with 60-70% reinvested to generate future growth. In the past five years the payout ratio has been at the upper end of that range, actually exceeding it in 1980, averaging 35.6% for the period.

Return on assets and equity have exhibited relative stability, averaging 8.8% and 21.9%, respectively. Combined has historically achieved a relatively high rate of return on stockholders' equity (ROE), which ranged between 21% and 23% in the past six years. The *Forbes 33rd Annual Report on American Industry* ranked the company second among sixteen selected life insurance companies, based on Combined's five-year average ROE of 21.8%. Overall, that performance put the company in the top 18% of the 1,040 companies rated.

For the past two years the trends have been mixed and less positive. On one hand, operating problems and the measures to solve them have resulted in pressure on direct premiums. On the other hand, investment results have reflected higher market yields and timely investment strategies.

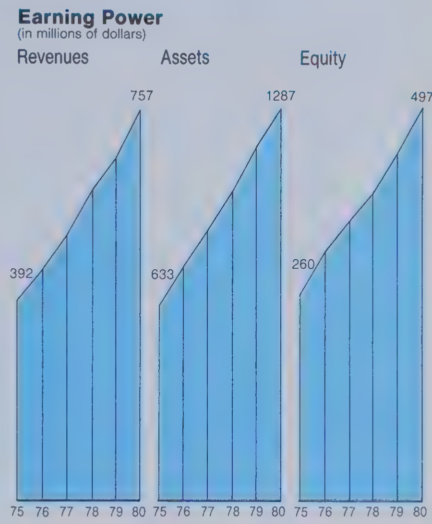
The 14.3% and 10.6% revenue gains in 1980 and 1979, respectively, reflect a significant shift in revenue mix because:

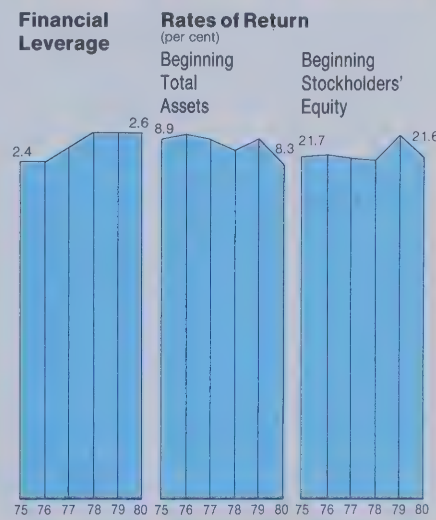
- Direct premiums earned increased 5.5%, the slowest rate in our history.
- Reinsurance premiums expanded at a record rate of 118.6%, and
- Investment income also increased at a rapid rate of 37.7%.

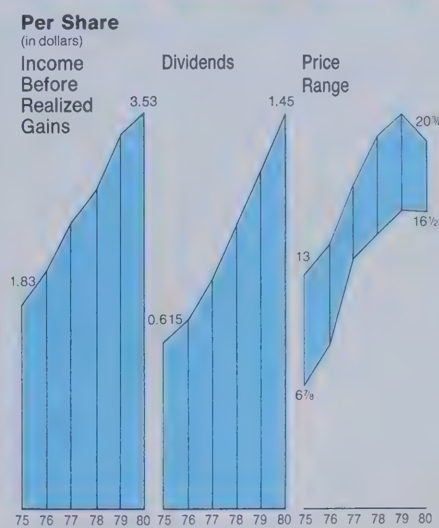
	Percent of Total Revenue	
	1980	1979
Premiums Earned:		
Direct	78.3%	84.9%
Reinsurance	9.3	4.8
Net investment income	12.4	10.3

Assets rose 11.2% in 1980 from rapid expansion of invested assets, as well as the growth of deferred acquisition costs, the other major asset.

	Asset Growth Rates	
	1980	1979
Investments	9.7%	14.7%
Deferred Acquisition Costs	14.0	11.2







Return on assets remained at the trend rate, despite pressure on underwriting profitability and adverse foreign exchange adjustments. The investment yield increased to 9.76% from 8.01% offsetting much of this pressure.

Last year, return on equity declined because of the increase in book value from nonoperating sources and the pressure on operating margins.

	Rates of Return	
	1980	1979
Beginning assets	8.3%	8.9%
Beginning equity	21.6	23.2

Earnings per share before security transactions were up only 4.9% following a 17.5% increase in 1979. Some significant changes in growth and profit trends are likely to occur in the early years of the 1980's; in particular, the reemphasis of our traditional marketing system as well as the introduction of new products and the expansion to new markets will likely cause premiums to improve at higher rates of growth in all divisions. At the same time the rate of increase of investment income will probably slow from the dramatic growth of the last two years, primarily due to the anticipated reduction in interest rates.

The control of general expenses will remain an important concern in the near term. The continued existence of rapid inflation, as well as our plans for expansion, require improved cost control. Specific plans for more stringent cost control are being made and should keep general expenses at more appropriate levels.

The tax rate will continue to climb in the early 1980's as investment income continues to increase in relation to total taxable income. However, renewed vigor in our insurance operations as well as a move toward more tax sheltered securities should moderate the rise in the tax rate in the next few years.

There is a general anticipation that both premiums and investments will generate double digit revenue increases in the early 1980's. This is exclusive of any consideration of additional revenues coming from acquisitions.

The Past Two Years in Detail

The adjacent variance analysis and the accompanying text deal with the operating results of 1980 and 1979, showing year to year dollar and percentage changes in the principal determinants of income per share before realized investment gains.

1980-1979 Comparisons

Premiums earned increased 11.6%, reflecting the individual performance of the various marketing divisions as follows:

	Premiums Earned Increase (Decrease)	
	1980	1979
USA A&H	(0.3)%	7.5%
USA Life	6.8	8.4
International A&H and Life	18.5	19.7
Agency	21.8	6.9
Reinsurance*	124.2	(9.7)
Other	(2.6)	14.8
Total	11.6%	8.6%

**Excludes Agency reinsurance.*

International operations showed an 18.5% rate of growth, which was favorable although down from 19.7% in 1979. USA Life recorded a 6.8% rate of growth, due in a large part to the adjustable life policy. Domestic A&H, however, showed a 0.3% decrease in premiums earned due to manpower deficiencies in the early part of the year.

Agency Division realized the most rapid premium growth in its history—21.8%, due to new rate structures as well as new business.

Reinsurance premiums rose 124.2%. The company's favorable financial position allowed it to take advantage of several attractive reinsurance treaties. Although reinsurance premiums do not generate the same high profit margin as do direct premiums, they do produce an attractive profit in relation to funds invested.

Investment income rose more than 37%. This pronounced growth reflects continued high cash flow and continued emphasis on short-term, high yield instruments. Also contributing significantly was a major real estate transaction which is discussed in more detail elsewhere in this report.

Policyholder benefits increased 13.7%, a more rapid rate of growth than premiums earned. This reflects higher benefit ratios in the domestic product lines.

Commissions and general expenses increased 16.7%. General expenses increased much faster than premiums earned due to inflation and expansion.

There was a significant foreign exchange loss of $2.4 million, mostly due to contracts in U.K. currency, which was highly volatile during the year.

The tax provision increased 13.5%, raising the effective rate to 25.3% from 23.9% primarily because investment income, which is taxed at a higher rate, was a larger portion of total income.

Variance Analysis

(000 Omitted)	1980 Amount	1980 Amount Increase	1980 Percent Increase	1979 Amount	1979 Amount Increase	1979 Percent Increase
Premiums Earned	**$663,176**	**$68,813**	**11.6%**	$594,363	$46,919	8.6%
Investment Income—Net	**93,813**	**25,689**	**37.7**	68,124	16,699	32.5
Total Revenue Earned	**$756,989**	**$94,502**	**14.3%**	$662,487	$63,618	10.6%
Policyholder Benefits	**$316,054**	**$38,015**	**13.7%**	$278,039	$12,423	4.7%
Commissions and General Expenses	**310,618**	**44,372**	**16.7**	266,246	30,883	13.1
Total Benefits and Expenses	**$626,672**	**$82,387**	**15.1%**	$544,285	$43,306	8.6%
Gain or (Loss) on Foreign Exchange	**(2,356)**	**(3,327)**	**—**	971	1,959	—
Income Before Income Tax and Realized Investment Gains	**$127,961**	**$ 8,788**	**7.4%**	$119,173	$22,271	23.0%
Provision for Income Tax	**32,346**	**3,846**	**13.5**	28,500	7,985	38.9
Income Before Realized Investment Gains	**$ 95,615**	**$ 4,942**	**5.5%**	$ 90,673	$14,286	18.7%
Per Share	**$3.53**	**0.16**		$3.37	0.51	
Realized Investment Gains	**1,378**	**1,045**	**313.8**	333	(711)	(68.1)
Per Share	**0.05**	**0.04**		0.01	(0.03)	
Net Income	**$ 96,993**	**$ 5,987**	**6.6%**	$ 91,006	$13,575	17.5%
Per Share	**$3.58**	**$ 0.20**		$3.38	$ 0.48	
Average Shares Outstanding	**27,099,792**			26,949,962		

Although net realized investment gains were only $1.4 million, they represented significantly larger gains, especially from the sale of real estate, substantially offset by losses purposely realized to improve the quality of the bond and preferred stock portfolios.

In summary, 1980 exhibited extremely rapid growth in revenue from investments and reinsurance, offset by a slowdown in direct insurance operations. It was also characterized by substantially higher general expenses, partly from planned outlays for future growth.

1979—1978 Comparisons

Premiums earned grew 8.6%, less than the 16.2% gain in 1978, primarily because of slower premium growth in Domestic A&H. Investment income, on the other hand, rose sharply, up 32.5%, due chiefly to the higher yields in short-term securities.

Overall benefit experience improved with such costs increasing only 4.7%. Commissions and general expenses, however, were up 13.1% due in large part to inflationary cost pressures. There were gains in foreign exchange, both in foreign asset exposure and in currency contracts.

The tax provision increased 38.9%, resulting in a 23.9% effective tax rate compared to 21.2% in 1978. The higher rate reflects the larger portion of income generated by investment activity in 1979 as well as the move to investment instruments with fully taxable income to take advantage of high yields in the short-term money market.

Inflation Effects

To illustrate the effects of general inflation, the following supplementary financial information is expressed in terms of average 1980 dollars by applying the "Consumer Price Index for All Urban Customers" to reported results shown. No specific adjustments have been made to property and equipment since these assets are immaterial to Combined's financial position.

The loss in purchasing power results from holding net monetary assets during a period when prices are increasing. The purchasing power loss does not represent an actual or expected disbursement of cash. Therefore, it does not decrease funds available for investment or payment of dividends. Net monetary assets comprise cash and claims to cash that are fixed in dollars less liabilities that are fixed in dollars. Combined considers all its assets other than equity securities and property and equipment to be monetary. All liabilities are deemed to be monetary.

	Years ended December 31				
	1980	1979	1978	1977	1976
Total Revenue Earned (000)					
As Reported					
As Adjusted	**$756,989**	$662,487	$598,869	$511,801	$446,482
Cash Dividends Per Share	**756,989**	752,078	756,402	695,937	646,286
As Reported					
As Adjusted	**$1.45**	$1.25	$1.05	$0.85	$0.695
Market Price Per Share at Year-End	**1.45**	1.42	1.33	1.16	1.01
As Reported	**$17.625**	$19.125	$17.875	$16.75	$14.375
As Adjusted	**16.834**	20.531	21.742	22.213	20.354
Total Stockholders' Equity (000)					
As Reported	**$497,379**	$442,860	$390,121	$354,731	$317,110
As Adjusted	**475,051**	475,415	474,529	470,433	449,012
Net Income (000)					
As Reported	**$ 96,993**	$ 91,006	$ 77,431	$ 72,447	$ 59,611
As Adjusted	**96,993**	103,313	97,799	98,512	86,287
Net Income Per Share					
As Reported	**$3.58**	$3.38	$2.90	$2.73	$2.25
As Adjusted	**3.58**	3.84	3.66	3.71	3.26
Loss in Purchasing Power on Net Monetary Assets (000)	**$ (24,637)**	$(23,624)	$(11,947)	$(8,707)	$(7,284)
Average Consumer Price Index (1967=100)	**246.8**	217.4	195.4	181.5	170.5

Financial Structure and Condition

The first measure of liquidity in an insurance company is essentially a comparison of future claims (represented by policy liabilities) and assets available to meet them (represented by invested assets). The adequacy of the reserves to meet future claims is scrutinized by the company, its auditors and the regulatory agencies. The determination is made by comparing prior reserving practices with subsequent claims experience. When and if reserves are found to be inadequate on the basis of experience, a company levies a charge against current income to restore reserve adequacy.

Assuming that reserves are adequate, a secondary measure of liquidity is the ease with which the company can convert invested assets to cash (preferably without realizing a loss), reflected in the maturity schedule and the amount of short-term investments in the portfolio.

Since premiums are paid in advance, operating funds are readily available. In fact, an established profitable insurance company often has substantial surplus capital resources in the form of earnings reinvested in the business. The bulk of the earnings are generated by Combined Insurance, but such earnings are only available to the company when distributed as dividends. Such dividends can only be made from the statutory unassigned surplus of Combined Insurance which amounted to $252.7 million and $255.2 million at December 31, 1980 and 1979, respectively. In addition, only a portion of this surplus (amounting to $57.2 million and $63.9 million at December 31, 1980 and 1979, respectively) can be distributed as dividends without incurring additional tax liability. Nevertheless, the company does have substantial unused lines of credit or borrowing power based on accumulated stockholders' equity which may be used to finance future growth.

Funds provided from operations were $183.5 million in 1980 and $192.3 million in 1979. The largest portion was applied to invested assets which increased $87.8 million in 1980 compared to $115.8 million in 1979. The somewhat smaller increase in 1980 followed the decline in premium growth while general expenses increased rapidly. The substantial fund flow to investments, although down modestly in 1980, was a key contributor to the rapid growth in investment income.

The mix of invested assets has changed over the two-year period. The proportion of preferred stock has declined to 7.5% and that invested in common stock and invested cash has decreased to 14.1% and 11.5%, respectively. The proportion of bonds and notes has increased to 60.8%, a change which has enhanced the liquidity of invested assets. Thus, at year-end 1980, over 25% of total assets were readily convertible to cash, giving flexibility to take advantage of rapid increases in interest rates.

The other major asset category is deferred and prepaid policy acquisition costs. Consistent with the matching principle (see footnote 1 to the consolidated financial statements), costs of acquiring business are deferred and reflected as expenses (or amortized) over the expected premium paying period of the policies. The increase in this asset was $23.7 million in 1980 vs $16.9 million in 1979. Amortization of the deferred portion amounted to $30.1 million in 1980 and $26.9 million in 1979.

Policy liabilities represent accumulated charges against income to provide adequate funds (held as investments) along with future premiums to pay current and future claims on outstanding policies. The net addition to reserves each year is a non cash expense which allows funds to be available for investments. Such liabilities increased $68.6 million compared to $69.5 million in 1979.

Policy liabilities (or reserves) are of three general types. The underlying purpose and principles for their establishment are described in the chart below:

Liability	Purpose	Reserving Principle
Future Policy Benefits	To provide for the present value of the excess of future assumed benefits over future net premiums	The present value is based on estimated future investment yield, mortality, morbidity and persistency.
Policy and Contract Claims	To reflect reported as well as incurred but not reported claims.	Estimates are based on current conditions and prior years' developments of amounts due on claims reported and unpaid as well as claims incurred but not reported.
Unearned and Advance Premium	To provide for premiums paid but not yet earned	Gross premiums collected are prorated between earned and unearned based on the period for which premium is paid.

Reserve adequacy is monitored by comparing expected with actual claims. The process has been effective and there has been no need for unusually large corrective charges to earnings.

Selected Data 1975–1980

($ in millions)

	Compound Growth Rate 1975/80	**1980**	1979	1978	1977	1976	1975
Income Statement Data							
Premiums Written	12.5%	**$ 676**	$ 604	$ 559	$492	$431	$375
Increase in Unearned And Advance Premiums	7.6	**13**	10	12	21	17	9
Premiums Earned	12.6%	**$ 663**	$ 594	$ 547	$471	$414	$366
Investment Income—Net	29.3	**94**	68	52	41	33	26
Total Revenue Earned	14.1%	**$ 757**	$ 662	$ 599	$512	$447	$392
Policyholder Benefits	12.5%	**$ 316**	$ 278	$ 266	$230	$201	$175
Commissions and General Expenses	14.9	**311**	266	235	201	175	155
Total Benefits and Expenses	13.7%	**$ 627**	$ 544	$ 501	$431	$376	$330
Gain or (Loss) on Foreign Exchange	—	**(2)**	1	(1)	—	—	(2)
Income Before Income Tax and Realized Investment Gains	16.4%	**$ 128**	$ 119	$ 97	$ 81	$ 71	$ 60
Provision For Income Tax	23.8	**32**	28	21	12	14	11
Income Before Realized Investment Gains	14.4%	**$ 96**	$ 91	$ 76	$ 69	$ 57	$ 49
Realized Investment Gains	—	**1**	—	1	3	3	—
Net Income	14.6%	**$ 97**	$ 91	$ 77	$ 72	$ 60	$ 49
Balance Sheet Data							
Assets							
Investments	15.5%	**$ 991**	$ 903	$ 787	$684	$588	$483
Cash and Receivables	26.4	**71**	53	46	39	36	22
Deferred and Prepaid Policy Acquisition Costs	14.8	**193**	169	152	135	114	97
Net Property and Equipment and Other	0.6	**32**	32	30	29	31	31
Total Assets	15.2%	**$1,287**	$1,157	$1,015	$887	$769	$633
Liabilities and Stockholders' Equity							
Future Policy Benefits	23.5%	**$ 333**	$ 289	$ 237	$187	$149	$116
Policy and Contract Claims	14.7	**135**	124	116	96	80	68
Unearned and Advance Premiums	12.2	**165**	151	141	129	109	93
Total Policy Liabilities	18.0%	**$ 633**	$ 564	$ 494	$412	$338	$277
Accrued Income and Other Taxes	15.1%	**$ 105**	$ 97	$ 84	$ 73	$ 63	$ 52
Commissions and General Expenses	17.4	**29**	28	26	21	16	13
Other Liabilities	(5.8)	**23**	25	21	26	35	31
Total General Liabilities	10.3%	**$ 157**	$ 150	$ 131	$120	$114	$ 96
Stockholders' Equity	13.8%	**$ 497**	$ 443	$ 390	$355	$317	$260
Total Liabilities and Stockholders' Equity	15.2%	**$1,287**	$1,157	$1,015	$887	$769	$633
Change in Financial Position Data							
Funds Provided							
Net Income	14.6%	**$ 97**	$ 91	$ 77	$ 72	$ 60	$ 49
Increase in Policy Liabilities	9.9	**69**	70	83	74	63	43
Amortization of Deferred Policy Acquisition Costs	13.4	**30**	27	24	21	20	16
Other—Net	—	**(12)**	4	12	9	8	8
Funds Provided from Operations	9.7%	**$ 184**	$ 192	$ 196	$176	$151	$116
From Common Stock Issued and Other	—	**(1)**	6	2	—	8	4
	8.8%	**$ 183**	$ 198	$ 198	$176	$159	$120
From Investments Sold or Matured	47.7	**730**	261	351	388	194	104
Total Funds Provided	32.4%	**$ 913**	$ 459	$ 549	$564	$353	$224
Funds Used							
Cost of Investments Purchased	35.7%	**$ 811**	$ 375	$ 467	$494	$283	$176
Additions to Deferred Policy Acquisition Costs	11.4	**48**	40	40	35	32	28
Cash Dividends to Stockholders	19.5	**39**	34	28	23	18	16
Other—Net	29.2	**18**	11	20	16	10	5
Increase or (Decrease) in Cash	—	**3**	(1)	(6)	(4)	10	(1)
Total Funds Used	32.4%	**$ 913**	$ 459	$ 549	$564	$353	$224

	1980	1979	1978	1977	1976	1975
Per Share Income						
Direct Premiums Earned	**$ 21.89**	$ 20.86	$ 19.20	$ 16.94	$ 15.10	$ 13.34
Reinsurance Premiums Earned	**2.58**	1.19	1.31	.83	.51	.47
Investment Income—Net	**3.46**	2.53	1.93	1.53	1.23	.98
Total Revenue Earned	**$ 27.93**	$ 24.58	$ 22.44	$ 19.30	$ 16.84	$ 14.79
Policyholder Benefits	**$ 11.66**	$ 10.32	$ 9.95	$ 8.69	$ 7.56	$ 6.60
Commissions and General Expenses	**11.46**	9.87	8.82	7.56	6.63	5.86
(Gain) or Loss on Foreign Exchange	**.09**	(.04)	.04	—	—	.07
Provision for Income Tax	**1.19**	1.06	.77	.46	.51	.43
Income Before Realized Investment Gains	**$ 3.53**	$ 3.37	$ 2.86	$ 2.59	$ 2.14	$ 1.83
Realized Investment Gains	**.05**	.01	.04	.14	.11	.01
Net Income	**$ 3.58**	$ 3.38	$ 2.90	$ 2.73	$ 2.25	$ 1.84
Stock Data						
Dividends Per Share	**$ 1.45**	$ 1.25	$ 1.05	$ .85	$ .695	$ .615
Stockholders' Equity Per Share	**$ 18.35**	$ 16.36	$ 14.53	$ 13.37	$ 11.96	$ 9.80
Price Range	**20⅜–16½**	21⅞–16⅝	20¾–15¼	18–13⅞	14¾– 9⅛	13– 6⅞
Average Shares	**27,099,792**	26,949,962	26,691,705	26,515,656	26,508,138	26,510,150
Common Stockholders	**27,849**	28,800	30,357	31,837	32,904	35,438
Ratio Analysis						
Pretax Return on Total Beginning Assets	**11.1%**	11.7%	10.9%	10.5%	11.1%	11.1%
Effective Tax Rate	**25.3%**	23.9%	21.2%	15.1%	19.3%	19.1%
Return on Total Beginning Assets	**8.3%**	8.9%	8.6%	8.9%	9.0%	8.9%
Financial Leverage ($ Assets Per $ Stockholders' Equity)	**2.6**	2.6	2.6	2.5	2.4	2.4
Return on Beginning Equity	**21.6%**	23.2%	21.5%	21.7%	21.8%	21.7%
Retention Rate (% Income Reinvested)	**58.9%**	62.8%	63.3%	67.2%	67.5%	66.4%

Direct Accident and Health Operating Statements

(000 Omitted) Years ended December 31	1980	1979
Revenue		
Premiums written		
Superior Policy Division—USA	**$332,251**	$334,361
Superior Policy Division—International	**109,706**	96,258
Agency Division	**37,496**	31,082
All other	**5,127**	5,357
Total premiums written	**$484,580**	$467,058
Less increase in unearned and advance premiums	**1,098**	3,526
Premiums earned	**$483,482**	$463,532
Investment income—net of expenses†	**61,448**	45,779
Total revenue earned	**$544,930**	$509,311
Percent increase over prior year	**7.0%**	11.0%
Benefits and Expenses		
Benefits to policyholders	**$189,602**	$178,549
Increase in future policy benefits	**10,761**	11,403
Commissions	**89,036**	86,568
General expenses	**119,668**	103,757
Amortization of deferred policy acquisition costs	**22,924**	22,385
Dividends to policyholders	**2,640**	3,646
Total benefits and expenses	**$434,631**	$406,308
Gain or (loss) on foreign exchange	**(1,684)**	741
Operating Income Before Income Tax	**$108,615**	$103,744
Percent increase over prior year	**4.7%**	22.1%

† *Investment income—net is allocated to direct accident and health and direct life operations in proportion to policy liabilities and stockholders' equity.*

Direct Life Operating Statements

(000 Omitted) Years ended December 31	1980	1979
Revenue		
Premiums written		
Superior Policy Division—USA	**$ 91,285**	$ 85,227
Superior Policy Division—International	**18,143**	13,314
All other	**2,193**	1,950
Total premiums written	**$111,621**	$100,491
Less increase in unearned and advance premiums	**2,003**	1,715
Premiums earned	**$109,618**	$ 98,776
Investment income—net of expenses†	**32,365**	22,345
Total revenue earned	**$141,983**	$121,121
Percent increase over prior year	**17.2%**	15.3%
Benefits and Expenses		
Benefits to policyholders	**$ 33,473**	$ 27,203
Increase in future policy benefits	**39,806**	38,292
Commissions	**12,412**	10,333
General expenses	**32,576**	26,922
Amortization of deferred policy acquisition costs	**6,121**	4,499
Total benefits and expenses	**$124,388**	$107,249
Gain or (loss) on foreign exchange	**(672)**	230
Operating Income Before Income Tax	**$ 16,923**	$ 14,102
Percent increase over prior period	**20.0%**	32.9%

Quarterly Financial Data

(000 Omitted)

	1980				
	1Q	2Q	3Q	4Q	Year
Direct Premiums Earned	$144,814	$148,143	$147,621	$152,522	$593,100
Reinsurance Premiums Earned	8,382	17,495	31,953	12,246	70,076
Investment Income—Net	20,667	20,947	22,600	29,599	93,813
Total Revenue Earned	$173,863	$186,585	$202,174	$194,367	$756,989
Income Before Realized Investment Gains or (Losses)	$ 20,367	$ 24,275	$ 21,019	$ 29,954	$ 95,615
Per Share	$0.75	$0.90	$0.78	$1.10	$3.53
Net Income	$ 21,040	$ 25,320	$ 21,410	$ 29,223	$ 96,993
Per Share	$0.78	$0.93	$0.79	$1.08	$3.58
Dividends Paid Per Share	$0.35	$0.35	$0.35	$0.40	$1.45
Stockholders' Equity Per Share	$ 15.62	$ 17.89	$ 17.72	$ 18.35	$ 18.35
Price Range	20⅜–16½	20⅜–17	20⅜–19⅛	19¾–16⅞	20⅜–16½
Average Yield	7.6%	7.5%	7.1%	8.7%	7.9%
Average Shares	27,079,926	27,104,907	27,108,677	27,108,677	27,099,792
Average Monthly Trading Volume	697,123	533,177	720,792	669,499	655,148

	1979				
	1Q	2Q	3Q	4Q	Year
Direct Premiums Earned	$134,464	$139,848	$141,791	$146,205	$562,308
Reinsurance Premiums Earned	6,334	7,247	6,586	11,888	32,055
Investment Income—Net	15,688	15,886	17,528	19,022	68,124
Total Revenue Earned	$156,486	$162,981	$165,905	$177,115	$662,487
Income Before Realized Investment Gains or (Losses)	$ 18,422	$ 22,579	$ 23,104	$ 26,568	$ 90,673
Per Share	$0.69	$0.84	$0.85	$0.98	$3.37
Net Income	$ 18,577	$ 22,987	$ 24,607	$ 24,835	$ 91,006
Per Share	$0.69	$0.86	$0.91	$0.92	$3.38
Dividends Paid Per Share	$0.30	$0.30	$0.30	$0.35	$1.25
Stockholders' Equity Per Share	$ 15.15	$ 15.63	$ 16.24	$ 16.36	$ 16.36
Price Range	18⅝–16⅝	21⅛–16⅞	21⅞–18½	21½–18½	21⅞–16⅝
Average Yield	6.8%	6.3%	5.9%	7.0%	6.5%
Average Shares	26,861,502	26,923,282	26,984,292	27,031,886	26,949,962
Average Monthly Trading Volume	813,143	730,075	523,567	613,667	670,113

Consolidated Statements of Income

(000 Omitted)	Years ended December 31		
	1980	1979	1978
Revenue			
Premiums earned			
Accident and health	**$ 483,482**	$ 463,532	$ 423,921
Life	**109,618**	98,776	88,691
Reinsurance (note 13)	**70,076**	32,055	34,832
Total premiums earned	**$ 663,176**	$ 594,363	$ 547,444
Investment income—net of expenses 1980—$5,856; 1979—$4,412; 1978—$3,686 (note 3)	**93,813**	68,124	51,425
Total revenue earned	**$ 756,989**	$ 662,487	$ 598,869
Benefits and Expenses			
Death and other benefits			
Accident and health	**$ 189,602**	$ 178,549	$ 169,556
Life	**33,473**	27,203	22,766
Increase in future policy benefits			
Accident and health	**10,761**	11,403	8,080
Life	**39,806**	38,292	36,166
Commissions	**101,448**	96,901	88,645
General expenses	**152,244**	130,730	113,681
Reinsurance benefits and expenses	**67,653**	30,677	33,418
Amortization of deferred policy acquisition costs (note 5)	**29,045**	26,884	23,982
Dividends to policyholders	**2,640**	3,646	4,685
Total benefits and expenses	**$ 626,672**	$ 544,285	$ 500,979
Gain or (loss) on foreign exchange	**(2,356)**	971	(988)
Income Before Income Tax and Realized Investment Gains	**$ 127,961**	$ 119,173	$ 96,902
Provision for income tax (note 7)			
Current	**22,485**	18,588	11,050
Deferred	**9,861**	9,912	9,465
Income Before Realized Investment Gains	**$ 95,615**	$ 90,673	$ 76,387
Realized investment gains—net of tax (note 4)	**1,378**	333	1,044
Net Income (note 12)	**$ 96,993**	$ 91,006	$ 77,431
Per Share			
Income before realized investment gains	**$3.53**	$3.37	$2.86
Realized investment gains—net of tax	**0.05**	0.01	0.04
Net income	**$3.58**	$3.38	$2.90
Cash dividends declared and paid	**$1.45**	$1.25	$1.05
Average outstanding shares	**27,099,792**	26,949,962	26,691,705

See accompanying notes to consolidated financial statements.

Consolidated Statements of Financial Position

(000 Omitted)	As of December 31	
	1980	1979
Assets		
Investments—Other than Investments in Affiliates (note 2)		
Bonds and notes—at amortized cost:		
(market: 1980—$527,121; 1979—$474,122)	**$ 603,060**	$ 518,573
Stock—at cost:		
Preferred (market: 1980—$2,342; 1979—$1,425)	**3,553**	2,182
Stock—at market:		
Preferred (cost: 1980—$119,007; 1979—$110,190)	**70,367**	73,373
Common (cost: 1980—$121,349; 1979—$154,471)	**139,624**	164,643
Mortgage loans on real estate	**34,897**	15,915
Real estate (net of accumulated depreciation: 1980—$2,443; 1979—$2,209)	**5,194**	5,278
Policy loans and other	**20,644**	14,794
Invested cash	**113,449**	108,228
Total investments	**$ 990,788**	$ 902,986
Cash	**6,687**	4,122
Receivables		
Premiums and other (net of allowance for doubtful accounts:		
1980—$794; 1979—$527)	**41,473**	35,953
Accrued investment income	**22,401**	13,186
Total receivables	**$ 63,874**	$ 49,139
Deferred and Prepaid Policy Acquisition Costs (note 5)	**192,533**	168,838
Property and Equipment, at Cost		
Land and buildings	**23,090**	21,711
Furniture and equipment	**23,194**	21,993
Leasehold improvements	**2,649**	2,022
Sub-total	**$ 48,933**	$ 45,726
Less accumulated depreciation and amortization	**20,527**	17,877
Net property and equipment	**$ 28,406**	$ 27,849
Other Assets	**4,608**	4,289
Total Assets	**$1,286,896**	$1,157,223

See accompanying notes to consolidated financial statements.

(000 Omitted)

Liabilities and Stockholders' Equity	As of December 31 1980	1979
Future policy benefits (note 6)		
Life	$ 281,631	$ 249,436
Accident and health	50,778	39,532
Policy and contract claims	134,979	123,859
Unearned and advance premiums		
Life	26,067	25,911
Accident and health	139,055	125,149
Accrued income tax (note 7)		
Current	16,803	17,166
Deferred	81,664	73,762
Commissions and general expenses	29,277	28,382
Other taxes	5,893	6,117
Other liabilities	23,370	25,049
Total Liabilities	$ 789,517	$ 714,363
Stockholders' Equity		
Preferred stock—no par value		
Class A—authorized and unissued—5,000,000 shares		
Class B—authorized and unissued—5,000,000 shares		
Common stock—$1 par value (note 11)		
Authorized—60,000,000 shares, issued	$ 27,109	$ 28,339
Paid-in additional capital	6	10,142
Net unrealized investment losses (notes 2 and 4)	(30,365)	(26,646)
Retained earnings (note 8)	500,629	444,991
Sub-total	$ 497,379	$ 456,826
Less cost of treasury stock: 1,268,100 shares	—	13,966
Total Stockholders' Equity	$ 497,379	$ 442,860
Total Liabilities and Stockholders' Equity	$1,286,896	$1,157,223

Consolidated Statements of Stockholders' Equity

(000 Omitted)	Years ended December 31		
	1980	1979	1978
Common Stock			
Balance at January 1	**$ 28,339**	$ 28,157	$ 27,845
Stock issued under officers' and employees' stock option plan	**—**	182	312
Elimination of treasury stock (note 1)	**(1,230)**	—	—
Balance at December 31	**$ 27,109**	$ 28,339	$ 28,157
Paid-In Additional Capital			
Balance at January 1	**$ 10,142**	$ 9,091	$ 7,236
Stock issued or disbursed from treasury under officers' and employees' stock option plan	**132**	1,051	1,855
Elimination of treasury stock (note 1)	**(10,268)**	—	—
Balance at December 31	**$ 6**	$ 10,142	$ 9,091
Net Unrealized Investment Losses			
Balance at January 1	**$(26,646)**	$ (20,332)	$ (4,187)
Net unrealized investment losses	**(3,719)**	(6,314)	(16,145)
Balance at December 31	**$(30,365)**	$ (26,646)	$ (20,332)
Retained Earnings			
Balance at January 1	**$444,991**	$387,688	$338,320
Net income	**96,993**	91,006	77,431
Cash dividends to stockholders of $1.45 per share in 1980, $1.25 per share in 1979 and $1.05 per share in 1978	**(39,308)**	(33,703)	(28,063)
Elimination of treasury stock (note 1)	**(2,047)**	—	—
Balance at December 31	**$500,629**	$444,991	$387,688
Stockholders' Equity at December 31 Before Deduction of Treasury Stock	**$497,379**	$456,826	$404,604
Less cost of treasury stock			
Balance at January 1	**$ 13,966**	$ 14,483	$ 14,483
Stock disbursed under officers' and employees' stock option plan	**(421)**	(517)	—
Elimination of treasury stock (note 1)	**(13,545)**	—	—
Balance at December 31	**$ —**	$ 13,966	$ 14,483
Stockholders' Equity at December 31	**$497,379**	$442,860	$390,121

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Financial Position

(000 Omitted)

	Years ended December 31		
	1980	1979	1978
Funds Provided			
From operations			
Net income	**$ 96,993**	$ 91,006	$ 77,431
Charges (credits) to income not affecting funds			
Future policy benefits	**43,441**	51,981	50,170
Policy and contract claims	**11,120**	7,324	20,756
Unearned and advance premiums	**14,062**	10,227	11,863
Amortization of premium and (discount) on securities	**(7,912)**	(7,131)	(4,800)
Increase in accrued investment income	**(9,215)**	(2,417)	(2,469)
Increase in prepaid policy acquisition costs	**(5,413)**	(3,797)	(1,078)
Amortization of deferred policy acquisition costs	**30,108**	26,884	23,982
Depreciation and amortization of property and equipment	**3,528**	2,913	2,873
Increase in accrued income tax	**7,539**	13,578	9,968
Other—net	**(763)**	1,717	7,185
Funds provided from operations	**$183,488**	$192,285	$195,881
From stock options exercised	**431**	1,582	2,167
Other—net	**(1,420)**	4,349	314
	$182,499	$198,216	$198,362
From investments sold or matured			
Bonds	**$317,919**	$ 77,366	$ 99,500
Preferred stock	**19,639**	3,026	53,386
Common stock	**365,499**	177,982	197,745
Mortgage loans	**26,982**	2,358	453
Funds provided from investments sold or matured	**$730,039**	$260,732	$351,084
Total Funds Provided	**$912,538**	$458,948	$549,446
Funds Used			
Cost of investments purchased			
Bonds and notes—net	**$392,381**	$159,777	$157,156
Preferred stock	**29,828**	1,806	22,935
Common stock	**332,377**	215,467	185,159
Mortgage and policy loans	**51,929**	7,587	9,252
Real estate	**445**	189	40
Invested cash—net	**4,295**	(9,661)	92,656
Total cost of investments purchased	**$811,255**	$375,165	$467,198
Additions to deferred policy acquisition costs	**48,157**	39,848	40,081
Additions to property and equipment	**4,649**	4,966	7,511
Cash dividends to stockholders	**39,308**	33,703	28,063
Other—net	**6,604**	6,110	13,025
Increase or (decrease) in cash	**2,565**	(844)	(6,432)
Total Funds Used	**$912,538**	$458,948	$549,446

See accompanying notes to consolidated financial statements.

1. Summary of Significant Accounting Principles and Practices

Principles of Consolidation

Combined International Corporation (the "Company") became the parent company and sole stockholder of Combined Insurance Company of America ("CICA") by a plan of exchange implemented on May 30, 1980. The stockholders of Combined Insurance Company of America were considered to have automatically exchanged their common shares on a one-for-one basis for the new parent company stock. The exchange has been accounted for as a pooling of interests; accordingly, the historical-cost basis of the assets and liabilities has not been changed. Treasury stock included in the accounts of CICA has been eliminated in consolidation by a charge to common stock for the par value. The amount in excess of par has been charged first to paid-in additional capital to the extent available and the remainder to retained earnings.

The accompanying consolidated financial statements include the accounts of Combined International Corporation, a holding company, and its wholly-owned operating subsidiary Combined Insurance Company of America and its totally-held subsidiaries. Unless the context indicates otherwise, the term "Combined" includes the Company and its affiliates while the term "Combined Insurance" includes CICA and its subsidiaries. All material intercompany accounts and transactions have been eliminated.

Basis of Presentation

These statements have been prepared in conformity with generally accepted accounting principles (GAAP). The significant differences between GAAP and statutory insurance accounting practices, which are used for reporting to regulatory authorities, are reflected in the reconciliation to statutory financial statements (note 12).

Investments

In the consolidated statements of financial position, investments in bonds are generally valued at amortized cost while most common and preferred stocks are valued at market. Common stock subject to call options is valued at the lower of exercise price or market value. Preferred stock which must be redeemed by the issuing enterprise or is redeemable at the option of Combined is valued at cost. The market values of stocks are determined in accordance with the methods prescribed by the National Association of Insurance Commissioners which approximate quoted market values.

Unrealized investment gains or losses are recorded directly in stockholders' equity, net of provision for the income tax which would be applicable if realized. Realized investment gains or losses are computed using specific costs of securities sold and are recorded in income net of applicable income tax. Realized call option premiums are reported as realized investment gains.

Foreign Currency Translation

Foreign assets are translated at current exchange rates except that deferred new policy acquisition costs and property and equipment are translated at historical exchange rates. Foreign liabilities are generally translated at current exchange rates. Revenues and expenses are translated at average exchange rates. Both realized and unrealized foreign exchange gains or losses are recorded in net income.

Recognition of Premium Revenue and Related Expenses

Premiums collected are reported as earned proportionately over the period covered by the policies. Most of the policies are sold and renewed on a six-month basis. Benefits and related expenses are associated with the premiums earned proportionately over the life of the policies through a provision for future policy benefit liabilities and through deferral and amortization of deferred and prepaid policy acquisition costs.

Deferred and Prepaid Policy Acquisition Costs

Costs of acquiring new business, principally the excess of new commissions over renewal commissions, and underwriting and sales expenses which vary with and are primarily related to the production of new business, are deferred and amortized over an assumed period which may not exceed the premium paying period of the policies. Amortization is related to and based upon the premiums expected to be earned on the policies. Such amortization is adjusted annually to reflect CICA's current withdrawal experience. Expected earned premiums are estimated by using the same assumptions used in estimating future policy benefits. For life insurance the costs are amortized over the premium paying period of the policy. About 50% of the initial acquisition cost on life insurance is amortized by the eighth policy year. Individual accident and health policy acquisition costs are amortized over ten to twenty years depending on observed withdrawal rates; 50% is amortized in three to five years. Group accident and health insurance acquisition costs are amortized equally over five years. Recurring costs of acquiring and renewing business which are prepaid are amortized as the related premium is earned.

Future Policy Benefit Liabilities and Unearned Premiums

Future policy benefit liabilities have been computed by the net level premium method based on estimated future investment yield, mortality, morbidity and withdrawal rates, which are based on CICA's experience using reasonable margins for adverse deviations. Unearned premiums are calculated using the pro rata method and are based on gross premiums.

Income Tax

CICA is taxed as a life insurance company and together with its eligible subsidiaries files a consolidated Federal income tax return. For Federal income tax purposes, foreign branch operations are included in the U.S. tax return. Such branches also file a separate tax return in the country in which they are located. Foreign tax credits reduce U.S. taxes to the extent of foreign taxes incurred.

Deferred income tax is provided for significant timing differences between financial reporting income and taxable income. Investment tax credits, which are insignificant, are reflected as a reduction of tax expense in the year they are recognized in the tax return.

2. Investments

Gross unrealized gains and (losses) resulting from valuation changes in marketable equity securities included in stockholders' equity at December 31, 1980 were $28,240,000 and $(58,605,000), respectively.

At December 31, 1980 and 1979, respectively, deferred investment income resulting from open or unexpired call options amounted to $6,111,000 and $5,757,000. Common stock encumbered by call options was valued at $36,401,000 and $53,471,000 at December 31, 1980 and 1979, respectively.

Loan commitments at year end 1980 amounted to $22,593,000. The contract amount and market value, respectively, of forward purchase commitments for Government National Mortgage Association pass-through certificates and Federal Home Loan Mortgage Corporation participation certificates amounted to $18,305,000 and $17,568,000 at December 31, 1980 and $234,000,000 and $218,589,000 at December 31, 1979. Unrealized gains and losses due to the differences between contract amount and market value are not reflected in the consolidated financial statements.

Securities and mortgage loans on deposit for regulatory authorities as required by law amounted to $56,799,000 at December 31, 1980 and $53,406,000 at December 31, 1979. Bonds pledged as collateral for Combined's forward purchase commitments of Government National Mortgage Association pass-through certificates and Federal Home Loan Mortgage Corporation participation certificates amounted to $759,000 and $15,805,000 at December 31,1980 and 1979,respectively.

Included in investments as of December 31, 1980 and 1979 were the following major security holdings (exclusive of U.S. government guaranteed securities) which exceeded 2% of total investments:

(000 Omitted)	1980	1979
American Telephone and Telegraph and Affiliates—		
Bonds	$23,393	$29,964
Preferred stock	3,506	1,760
Common stock	3,564	5,848

3. Investment Income

The components of investment income are as follows:

(000 Omitted) Years ended December 31	1980	1979	1978
Bonds and notes	$56,171	$37,802	$27,773
Preferred stock	9,657	8,590	10,830
Common stock	13,364	8,523	6,380
Mortgage loans on real estate	6,910	1,118	943
Real estate	1,576	1,072	964
Policy loans and other	914	805	1,367
Invested cash	11,077	14,626	6,854
Gross investment income	$99,669	$72,536	$55,111
Investment expenses	5,856	4,412	3,686
Net investment income	$93,813	$68,124	$51,425

Mortgage loan investment income for 1980 includes an accrual of $2,918,000 representing CICA's share of earnings related to a real estate investment in which CICA is entitled to 25% of the earnings of such investment in addition to the interest rate stated in the mortgage agreement. CICA's share of earnings is based on sales completed in 1980 and does not anticipate earnings expected in 1981.

4. Investment Gains and Losses

The components of realized and unrealized gains and (losses) on investments recognized in the consolidated financial statements are as follows:

(000 Omitted)

	Year ended December 31, 1980		
	Realized	Unrealized	Net
Bonds	$(16,590)	$ —	$(16,590)
Preferred stock	(3,926)	(11,822)	(15,748)
Common stock	6,888	8,103	14,991
Options closed or expired	962	—	962
Real estate	10,785	—	10,785
Other	4,179	—	4,179
Total before tax	$ 2,298	$ (3,719)	$ (1,421)
Less applicable tax	920	—	920
Total	$ 1,378	$ (3,719)	$ (2,341)

	Year ended December 31, 1979		
	Realized	Unrealized	Net
Bonds	$(4,021)	$ —	$ (4,021)
Preferred stock	(277)	(14,334)	(14,611)
Common stock	746	8,020	8,766
Options closed or expired	3,957	—	3,957
Other	166	—	166
Total before tax	$ 571	$ (6,314)	$ (5,743)
Less applicable tax	238	—	238
Total	$ 333	$ (6,314)	$ (5,981)

	Year ended December 31, 1978		
	Realized	Unrealized	Net
Bonds	$ (257)	$ 14	$ (243)
Preferred stock	(2,614)	(9,357)	(11,971)
Common stock	2,700	(6,802)	(4,102)
Options closed or expired	1,916	—	1,916
Other	15	—	15
Total before tax	$ 1,760	$(16,145)	$(14,385)
Less applicable tax	716	—	716
Total	$ 1,044	$(16,145)	$(15,101)

Unrealized market depreciation on bonds and preferred stock which must be redeemed by the issuing enterprise or is redeemable at the option of Combined amounted to $31,942,000, $11,860,000 and $18,430,000 in 1980, 1979 and 1978, respectively. Such market depreciation is not reflected in the consolidated financial statements.

5. Deferred and Prepaid Policy Acquisition Costs

The accounting treatment for deferred and prepaid policy acquisition costs and related amortization is described in note 1. A breakdown of costs deferred and related amortization by type of insurance follows:

(000 Omitted)	Life Insurance	Accident & Health Insurance	Total
1980			
Balance of deferred and prepaid policy acquisition costs, January 1	$ 42,464*	$126,607*	$169,071*
Deferred policy acquisition costs	10,629	37,528	48,157
Charged to costs and expenses	(5,583)	(19,112)	(24,695)
Balance of deferred and prepaid policy acquisition costs, December 31	$ 47,510	$145,023	$192,533
Initial premiums written	$ 15,226	$ 81,569	$ 96,795
Renewal premiums written	$143,868	$435,750	$579,618
1979			
Balance of deferred and prepaid policy acquisition costs, January 1	$ 36,812*	$115,265*	$152,077*
Deferred policy acquisition costs	9,183	30,665	39,848
Charged to costs and expenses	(2,511)	(20,576)	(23,087)
Balance of deferred and prepaid policy acquisition costs, December 31	$ 43,484	$125,354	$168,838
Initial premiums written	$ 13,531	$ 83,032	$ 96,563
Renewal premiums written	$105,165	$402,029	$507,194
1978			
Balance of deferred and prepaid policy acquisition costs, January 1	$ 31,869*	$102,845*	$134,714*
Deferred policy acquisition costs	7,413	32,668	40,081
Charged to costs and expenses	(2,483)	(20,421)	(22,904)
Balance of deferred and prepaid policy acquisition costs, December 31	$ 36,799	$115,092	$151,891
Initial premiums written	$ 18,026	$ 94,426	$112,452
Renewal premiums written	$ 83,395	$363,460	$446,855

*Portion of beginning balance revalued to end of period foreign exchange rates.

The largest single element of deferred policy acquisition costs relative to life insurance was the excess of new commissions over renewal commissions amounting to $7,186,000, $5,940,000 and $5,771,000 for 1980, 1979 and 1978, respectively. The largest single element of deferred policy acquisition costs relative to accident and health insurance was the excess of new commissions over renewal commissions amounting to $21,104,000, $20,011,000 and $21,811,000 for 1980, 1979, and 1978, respectively. The remaining costs, none of which exceeded 15% of deferred policy acquisition costs, were substantially comprised of the excess of new overrides over renewal overrides, policy issuance costs and underwriting costs.

6. Future Policy Benefits

The composition of future policy benefits and applicable interest assumptions by year of issue are presented below:

(000 Omitted) Type of Insurance	As of December 31 Future Policy Benefits 1980	1979	Years of Issue	Interest Rates
Ordinary life	$281,148	$249,052	1966 to date	6% decreasing over 20 years to 4.5%, 4.5% thereafter
Other life	483	384	1967 to date	3% all years
Individual accident & health	49,798	38,532	1969 to date	6% first 10 years, 5% second 10 years, 4.5% thereafter
/	980	1,000	Prior to 1969	4% first 10 years, 3.5% second 10 years, 3% thereafter
Total	$332,409	$288,968		

7. Income Tax

CICA and its eligible U.S. subsidiaries file a consolidated Federal income tax return under the provisions of the Life Insurance Income Tax Act of 1959. Taxable investment income is taxed at the standard corporate rate with realized investment gains or losses at applicable capital gain rates. One-half of taxable underwriting profits, if any, is taxed, with the remaining half accumulated in a memorandum "policyholders' surplus account." "Policyholders' surplus," which is taxed only when distributed to the Company or if it exceeds prescribed limits, approximated $224,900,000, $224,700,000 and $202,800,000 at year ends 1980, 1979 and 1978, respectively. The net additions to the "policyholders' surplus account" for the years ended December 31, 1980, 1979 and 1978 were approximately $200,000, $21,900,000 and $21,700,000, respectively. It is not CICA's intention to distribute "policyholders' surplus" to the Company in the foreseeable future and no income tax provision has been made for that purpose. CICA has approximately $57,200,000 of retained earnings available for distribution to the Company at December 31, 1980 without incurring additional tax liability, compared to approximately $63,900,000 at December 31, 1979 (see note 8).

Foreign tax credit carryovers decreased for financial statement purposes by $2,004,000 in 1980, decreased by $55,000 in 1979 and increased by $300,000 in 1978. There are no foreign tax credit carryovers available as of December 31, 1980.

The components of the deferred income tax provisions are as follows:

(000 Omitted) Years ended December 31	1980	1979	1978
Approximate net level basis for valuing the direct ordinary life reserves	$ 5,758	$ 5,015	$ 3,789
Policy acquisition costs expensed for tax purposes and deferred or prepaid for financial accounting purposes	11,073	7,939	8,331
Tax basis increase in future policy benefit liabilities greater than the financial accounting increase			
A&H	2,199	2,293	3,678
Life	6,403	559	534
Special life insurance company deductions applied to reduce deferred tax	(9,166)	—	—
Special life insurance company deferral for one-half of the excess of gain from operations over taxable investment income	(6,392)	(7,485)	(7,334)
Other items—net	(14)	1,591	467
Total	$ 9,861	$ 9,912	$ 9,465

Differences between Combined's effective tax rate and the total "normal" Federal tax rate are as follows:

Years ended December 31	1980	1979	1978
"Normal" tax rate	46%	46%	48%
Decrease in tax resulting from			
Income subject to taxation only when distributed or exceeding prescribed limits ("policyholders' surplus account")	(6)	(11)	(11)
Tax exempt investment income deductions	(7)	(5)	(7)
Special deductions for nonparticipating policies and group life and A&H premiums	(6)	(6)	(8)
Other	(2)	—	(1)
Effective tax rate	25%	24%	21%

The provision for income tax is made up of the following components:

(000 Omitted)	Year ended December 31, 1980			
	U.S.			
	Federal	State	Foreign	Total
Current tax expense	$12,848	$ 423	$ 9,214	$22,485
Deferred tax expense	8,014	240	1,607	9,861
Total	$20,862	$ 663	$10,821	$32,346

	Year ended December 31, 1979			
	U.S.			
	Federal	State	Foreign	Total
Current tax expense	$10,868	$ 611	$ 7,109	$18,588
Deferred tax expense	8,794	—	1,118	9,912
Total	$19,662	$ 611	$ 8,227	$28,500

	Year ended December 31, 1978			
	U.S.			
	Federal	State	Foreign	Total
Current tax expense	$ 6,243	$ 440	$ 4,367	$11,050
Deferred tax expense	7,528	—	1,937	9,465
Total	$13,771	$ 440	$ 6,304	$20,515

The current tax expense for the year ended December 31, 1978 includes favorable adjustments applicable to prior years of $1,228,000.

8. Restrictions on Stockholders' Equity

The Company's ability to pay dividends to its stockholders is dependent on receipt of dividends from CICA. Statutory authorities allow payments of dividends to be made from statutory unassigned surplus only. Statutory unassigned surplus amounted to $252,650,000, $255,240,000 and $219,222,000 at December 31, 1980, 1979 and 1978, respectively.

See note 7 for possible tax effects of distributions made out of untaxed earnings.

9. Segment Information

The 1980, 1979 and 1978 segment information located on page 12 is incorporated herein by reference.

10. Profit Sharing and Pension Plans

Profit Sharing Plans

As of December 31, 1980, Combined Insurance maintained contributory profit sharing plans for the benefit of United States salaried and commissioned employees and for Canadian salaried employees and commissioned agents. For 1980, 1979 and 1978 Combined Insurance made aggregate provisions for all profit sharing plans of $6,948,000, $7,205,000 and $7,088,000, respectively.

Pension Plans

Combined Insurance's noncontributory qualified employees' pension plan provides benefits for substantially all salaried employees in the United States upon retirement, based on years of service and salary. As of January 1, 1980, the plan's net assets available for benefits were $5,941,000 and exceeded the actuarially computed value of vested benefits by $3,327,000. Combined Insurance's policy for funding pension costs is to fund all benefits accruing during the year and to amortize prior service costs over 30 years. The unfunded prior service cost as of January 1, 1980 was $3,977,000. As of January 1, 1980, the actuarial present values of vested and nonvested accumulated plan benefits were $2,523,000 and $842,000, respectively. An assumed rate of return of 7.5% was used in determining the present value of accumulated plan benefits. The pension plan provisions for 1980, 1979 and 1978 were $659,000, $817,000 and $777,000, respectively. Changes in actuarial assumptions reduced the 1980 plan provision by $256,000.

11. Stock Option Plans

The Company's stockholders approved a nonqualified stock option plan in 1980. During the year, options to purchase 895,175 shares of Company stock were granted at 100% of market value on the date of grant ($18.06). These options will first become exercisable (in part) in 1983. As of December 31, 1980, options to purchase 871,375 shares remained outstanding.

The qualified stock option plan expired on July 23, 1975 with the last outstanding options either expiring or being exercised by March, 1980. In 1980, 1979 and 1978, respectively, options were exercised for 38,210; 228,987 and 311,114 shares in the amounts of $431,000, $1,582,000 and $2,167,000.

12. Reconciliation to Statutory Financial Statements

A reconciliation of net income, as reported for statutory purposes, to that reported under GAAP is as follows:

(000 Omitted) Years ended December 31,	1980	1979	1978
Net income—statutory basis	$ 62,621	$ 82,345	$ 57,541
Adjustments			
Deferred policy acquisition costs	48,157	39,848	40,081
Amortization of deferred and prepaid policy acquisition costs	(24,695)	(23,087)	(22,904)
Future policy benefit liabilities			
Accident and health	3,529	3,867	12,410
Life	14,093	1,438	1,181
Deferred income tax	(9,861)	(9,912)	(9,465)
Gain or (loss) on foreign exchange	67	278	(595)
Realized investment gains or (losses)	448	(3,591)	(819)
Real estate interest	2,918	—	—
Other adjustments-net	(248)	(180)	1
Net income—Combined Insurance	$ 97,029	$ 91,006	$ 77,431
Net loss—Combined International	(36)	—	—
Net income as reported under GAAP herein	$ 96,993	$ 91,006	$ 77,431

A reconciliation of stockholders' equity follows:

(000 Omitted) As of December 31	1980	1979	1978
Stockholders' equity—statutory basis	$291,256	$293,426	$256,467
Mandatory securities valuation reserve	49,025	50,934	36,823
Sub-total	$340,281	$344,360	$293,290
Adjustments			
Deferred and prepaid policy acquisition costs	192,533	168,838	151,891
Valuation changes on preferred stock	(46,767)	(35,315)	(21,193)
Future policy benefit liabilities			
Accident and health	38,811	35,287	31,282
Life	310	(13,603)	(14,847)
Deferred income tax	(81,664)	(73,762)	(64,727)
Unauthorized reinsurance reserve credit	8,411	338	301
Assets non-admitted	17,574	17,103	14,524
Other adjustments-net	2,167	(386)	(400)
Stockholders' equity—Combined Insurance	$471,656	$442,860	$390,121
Stockholders' equity—Combined International	25,723	—	—
Stockholders' equity as reported under GAAP herein	$497,379	$442,860	$390,121

13. Reinsurance

In the ordinary course of business and in accordance with the practice prevailing in the insurance industry, Combined Insurance assumes reinsurance from other insurers. Combined Insurance does not cede a material amount of business to reinsurers. The following is a summary of pertinent information on reinsurance assumed net of ceded:

(000 Omitted)	Years ended December 31		
	1980	1979	1978
Accident and Health Insurance			
Premiums earned	$ 23,672	$ 15,817	$ 25,049
Premiums earned as a % of total accident and health premiums earned	4.7%	3.3%	5.6%
Life Insurance			
Premiums earned	$ 46,404	$ 16,238	$ 9,783
Premiums earned as a % of total life premiums earned	29.7%	14.1%	9.9%
Reinsurance in force (end of period)	$1,986,642	$1,313,694	$466,208
Reinsurance in force as a % of total in force (end of period)	32.0%	24.0%	9.6%

14. Litigation

Combined Insurance is defending lawsuits arising in the ordinary course of business from claims under insurance policies and from other matters. Accruals for these lawsuits have been provided to the extent that losses are deemed probable. Such accruals do not materially affect the consolidated financial statements. Certain of the lawsuits seek extraordinary damages. Management believes these claims to be without merit and, to date, has been successful in similar cases in settling for insignificant amounts, having the extraordinary damage aspects dismissed or defending to verdict without the imposition of such extraordinary damages.

15. Quarterly Financial Data (Unaudited)

The unaudited quarterly financial data on page 26 is incorporated herein by reference.

16. Financial Data Adjusted for General Inflation (Unaudited)

The inflation adjusted financial data included on page 20 is incorporated herein by reference.

Report of Independent Certified Public Accountants

The Board of Directors and Stockholders
Combined International Corporation:

We have examined the consolidated statements of financial position of Combined International Corporation and subsidiaries as of December 31, 1980 and 1979 and the related consolidated statements of income, stockholders' equity and changes in financial position for each of the years in the three year period ended December 31, 1980. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of Combined International Corporation and subsidiaries at December 31, 1980 and 1979 and the results of their operations and changes in their financial position for each of the years in the three year period ended December 31, 1980, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

Chicago, Illinois
February 12, 1981

Report by Management

The management of Combined strongly supports the concept of a statement informing stockholders of management's financial responsibilities. The following consolidated financial statements of Combined International Corporation and all information in the annual report are the responsibility of management. The statements have been prepared in conformity with generally accepted accounting principles appropriate to stock life insurance companies. Financial information elsewhere in this report is consistent with that in the financial statements. The consolidated financial statements have been audited by our independent accountants, Peat, Marwick, Mitchell & Co. Their role is to render an independent professional opinion on Combined's financial statements in accordance with generally accepted auditing standards.

Management maintains a system of internal controls designed to meet its responsibilities for reliable financial statements. This system is designed to provide reasonable assurance, at appropriate costs, that assets are safeguarded and that transactions are properly recorded and executed in accordance with management's authorization. Judgments are required to assess and balance the relative costs and expected benefits of those controls. In addition, management supports an extensive program of internal audits and maintains a professional staff of internal auditors who coordinate audit coverage with the independent accountants and conduct financial and operational audits.

The Board of Directors selects an Audit Committee from among its members. No member of the Audit Committee is or has been an employee of the Company. The Audit Committee is responsible to the Board for reviewing the accounting and auditing procedures and financial practices of the Company and for recommending appointment of the independent accountants. The Audit Committee meets periodically with management, internal auditors and independent accountants to review the work of each and satisfy itself that they are properly discharging their responsibilities. Both the independent accountants and the internal auditors have free access to the Committee, without the presence of management, to discuss their opinions on the adequacy of internal controls and to review the quality of financial reporting.

Board of Directors and Principal Officers of the Company and Subsidiaries

Board of Directors

W. Clement Stone (1,2,6)
Chairman of the Board and Founder

Clement Stone (1,2,3,6)
President and Chief Executive Officer

Dr. William J. Andrews (3,4,8)
Doctor of Medicine, Chairman of Department of Internal Medicine Swedish Covenant Hospital

Daniel T. Carroll (4,5,6,8)
President and Chief Executive Officer of Hoover Universal, Inc.

Gordon A. Dancer (1,2)
Executive Vice President

Ronald K. Holmberg (1,2)
Executive Vice President and Treasurer

Perry J. Lewis (3,4,5,6,7,8)
President of MacKay–Lewis, Inc.

Robert P. Neuschel (1,4,5,6,7,8)
Professor of Corporate Governance, J. L. Kellog Graduate School of Management and Managing Director of the Transportation Center, Northwestern University

Edmund G. Pabst

Peer Pedersen (1,3,4,5,6,7,8)
Senior Partner in Law Firm of Pedersen & Houpt

Raymond I. Skilling (1,2)
Executive Vice President

J. Milburn Smith (3,4,8)
Insurance Consultant

Board Committees

(1) Executive Committee
(2) Operating Committee
(3) Investment Committee
(4) Audit Committee
(5) Compensation Committee
(6) Nominating Committee
(7) Special Incentive Committee
(8) Committee on Organization

Abbreviations

SPD is Superior Policy Division
A&H is Accident and Health

Principal Officers

W. Clement Stone

Clement Stone

Gordon A. Dancer

Ronald K. Holmberg

Raymond I. Skilling

Wallace J. Buya
Vice President and Secretary

Principal Officers Combined Insurance Company of America and Subsidiaries

W. Clement Stone

Clement Stone

Gordon A. Dancer
Executive Vice President—Operations

Ronald K. Holmberg
Executive Vice President—Management

Raymond I. Skilling
Executive Vice President—Planning and Implementation

Robert Boyajian, Jr. (2)
Senior Vice President—National Sales Manager SPD–Life–USA

Victor R. Fernitz (2)
Senior Vice President—SPD–International Operations

Earl A. Forte (2)
President—Metro Division

J. Michael Hester
Senior Vice President—National Sales Manager SPD–A&H–USA

H. Robert Powell (3)
Senior Vice President—Asset Management

Kenneth D. Saunders (2)
Senior Vice President—Agency Division

Richard M. Ravin
Vice President—Divisional Manager—SPD–A&H–USA

Donald F. Veit
Vice President—Senior Divisional Manager—National Health Care Division SPD–A&H–USA

Bernard Chapados
Resident Vice President—France

Peter Cherian
Resident Vice President—Canadian Operations

Alastair Cumming
Resident Vice President—Japan

Paul Chilton
Vice President—Hawaiian Operations

C. Toby Perry
Resident Vice President—Australia and New Zealand

David R. Reynolds
Resident Vice President—United Kingdom

John A. Baker
Vice President and Director of Personnel

James C. Bard
Vice President—Asset Management

William Blackburn, Jr.
Vice President—National Staff SPD–A&H–USA

David Blake
Vice President—United Kingdom Administration

Paul Boudreau
Vice President—Operations Division

Derek Bright
Vice President—Administration—Pacific Division

Edward M. Burgh
Vice President—Corporate Taxes

Wallace J. Buya
Vice President, Secretary and Executive Assistant
to the Chairman

Rafael Chacon
Vice President—SPD–A&H–USA

Donald D. Clement
Vice President—Administrative Services

Robert A. Collien
Vice President and Treasurer
Combined Life Insurance Company of New York

Kenneth E. Conry
Vice President—Sales Administration SPD–A&H–USA

Michael Conway
Vice President—Asset Management

James Gigante
Vice President—SPD–A&H–USA

Richard J. Golden
Vice President—Data Processing

Tadao Ishizumi
Vice President—Sales—Japan

Richard Iwamura
Resident Vice President—Hawaii

Alan R. Johnson
Vice President and Assistant General Counsel

J. W. Johnson
Vice President—Underwriting

Spencer Koppel
Corporate Vice President and Actuary

Michael Lambrakos
Vice President
Combined Insurance Company of Wisconsin

George Lawler
Internal Auditor

J. Russell Lyday
Vice President
Combined American Insurance Company

Ronald D. Markovits
Vice President—International, Law and Government Relations

Donald D. McDonald
Vice President and Treasurer

Lawrence R. Miller
Vice President—Asset Management

Craig Monson
Vice President—Hearthstone Division

Herbert S. Moreland
Vice President—Claims

Graham Morgan
Vice President—Development–New Operations
International Operations

Edmund G. Pabst
Vice President and General Counsel

R. P. Patterson
Vice President—Agency Division

Kenneth R. Peters
Vice President—Agency Division Claims

Gerald H. Pugh
Vice President and Director of Government Relations

J. Duncan Randall
Vice President—Corporate Insurance

Robinson P. Rigg
Vice President—Public Relations

Michael J. Ritt, Jr.
Vice President—Communications

Leonard Rittner
Vice President—Hearthstone Division

Norbert Rocks
Vice President—Canadian Administration

Harold Solochek
Vice President—Administration
International Operations

J. V. Stone
Vice President

John Stone
Vice President—Consumer Affairs
and Internal Market Conduct

Michael P. Terry
Vice President—Field Accounting Services

James D. White
Controller

Combined International Corporation

Executive Offices
707 Combined Centre
Northbrook, Illinois 60062
Phone: 312-564-8000
Cable Address—Combined Telex No. 25-3364

Combined Insurance Company of America

Home Office

Operations
5050 N. Broadway
Chicago, Illinois 60640
Phone: 312-275-8000
Cable Address—Combined Telex No. 20-6114

Marketing and Management
707 Combined Centre
Northbrook, Illinois 60062
Phone: 312-564-8000
Cable Address—Combined Telex No. 25-3364

International Offices

Canadian Branch
980 Yonge Street
Toronto, Ontario M4W 2J9, Canada

United Kingdom Branch
15 Fairfield West, Kingston—Upon—Thames
Surrey KT1 2PA, England

Australian Branch
Combined Life Insurance Company of Australia Limited
132-138 Arthur Street
North Sydney, N.S.W., Australia 2060

New Zealand Branch
Tudor House, 333 Remuera Road
Remuera, Auckland 5, New Zealand

Combined Insurance Company of Ireland Limited
Merrion House
Merrion Road, Dublin 4, Ireland

West German Branch
Vereinigte Versicherungsgesellschaft von Amerika
Gustav-Stresemann-Ring 12-16
6200 Wiesbaden, West Germany

French Branch
149 Rue Montmartre
75002 Paris, France

Japanese Branch
Kowa Building #9
1-8-10 Akasaka
Minato-Ku, Tokyo, Japan

Domestic Subsidiaries and Branch

Combined American Insurance Company
3141 Hood Street, Dallas, Texas 75219

Combined Insurance Company of Wisconsin
104 S. Main Street, Fond du Lac, Wisconsin 54935

Combined Life Insurance Company of New York
Combined Life Insurance Building
18 Computer Drive, Albany, New York 12205

Hearthstone Division
111 Washington Street
Brookline, Massachusetts 02146

Combined Opportunities, Incorporated
300 North State Street, Chicago, Illinois 60610
(A Minority Enterprise Small Business
Investment Company)

CICA Realty Company
707 Combined Centre
Northbrook, Illinois 60062

The Company will file its Annual Report on Form 10-K with the Securities and Exchange Commission on or before March 31, 1981. A copy of the report, including the financial statements and schedules thereto, and a list describing all the exhibits not contained therein, may be obtained without charge by any stockholder. (The report will be available on or after March 31, 1981.) Requests for copies of the report should be sent to: Office of the Corporate Secretary, Combined International Corporation, 707 Combined Centre, Northbrook, Illinois 60062

Transfer Agent and Registrar

American National Bank and Trust Company
Chicago, Illinois 60690

Automatic Dividend Reinvestment Plan

American National Bank and Trust Company
Chicago, Illinois 60690

Annual Stockholders' Meeting

The Drake Hotel
140 East Walton
Chicago, Illinois
April 10, 1981 at 10:00 A.M.

Combined International Corporation
707 Combined Centre
Northbrook, Illinois 60062
312-564-8000

Form No. 100101-0